Jurisdictional Statement

81-1370

No. 81-

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY, INC.,
Appellee.

On Appeal from the Supreme Court of Kansas

JURISDICTIONAL STATEMENT

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QUESTIONS PRESENTED

1. Whether Section 4 of the Kansas Natural Gas Price Protection Act, Kan. Stat. Ann. § 55-1404 (Supp. 1980), violates the Contract Clause of the United States Constitution when the purpose and effect of the statute are to relieve a utility of its contractual obligation to pay price increases specified in long-term natural gas purchase contracts; when the statute does not further an important general social purpose; and when any limited public interest addressed by the statute could have been served by means that would not impair legitimate contractual rights.

2. Whether § 105(b)(1) of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3315(b)(1) (Supp. IV 1980), precludes the operation of contractually established price escalation clauses in intrastate natural gas contracts and freezes prices to those in effect on the date of enactment of the Natural Gas Policy Act.*

PARTIES BELOW

The only parties to this proceeding in the court below are those indicated by the caption of this jurisdictional statement. Appellant Energy Reserves Group, Inc., has no parent corporation, subsidiaries (except wholly-owned subsidiaries), or affiliates.

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* This question also is presented in *Mesa Petroleum Co.* v. *The Kansas Power & Light Co., petn. for cert. pending*, No. 81-711.

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ENERGY RESERVES GROUP, INC.,
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v.

THE KANSAS POWER AND LIGHT COMPANY, INC.,
Appellee.

On Appeal from the Supreme Court of Kansas

JURISDICTIONAL STATEMENT

Appellant Energy Reserves Group, Inc. ("ERG") appeals from a final judgment of the Supreme Court of Kansas.

OPINIONS BELOW

The opinion of the Kansas Supreme Court (App. 1a-24a)[1] is reported at 230 Kan. 176, 630 P.2d 1142 (1981). The opinions of the trial court on cross-motions for summary judgment (App. 25a-41a) and on ERG's motion to reconsider (App. 42a-44a) are unreported. The journal entry of the trial court (App. 45a-49a) is unreported.

JURISDICTION

The judgment of the Supreme Court of Kansas was entered on July 17, 1981. The Kansas Supreme Court denied rehearing on September 23, 1981 (App. 50a). Appellant filed a timely notice of appeal in the Kansas Supreme Court on December 8, 1981 (App. 51a-54a). Upon timely application, Justice White granted appellant an extension of time until January 21, 1981, to docket an appeal or, in the alternative, to file a petition for a writ of certiorari (App. 55a). The jurisdiction of this Court to

[1] Citations to "App." refer to the separate appendix that accompanies this jurisdictional statement, pursuant to Rule 15.1(j) of this Court.

review the judgment of the court below is conferred by 28 U.S.C. § 1257(2).[2]

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The following constitutional provisions and statutes involved are set forth in the appendix accompanying this statement: the Contract Clause of Article I, Section 10 of the United States Constitution (App. 56a); the relevant parts of §§ 102 and 105 of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3312 & 3315 (Supp. IV 1980) (App. 56a-58a); the Kansas Natural Gas Price Protection Act, Kan. Stat. Ann. §§ 55-1401 through 55-1415 (Supp. 1980) (App. 58a-65a), § 4 of which is involved in this case (App. 60a-61a).

STATEMENT OF THE CASE

A. Introduction.

This appeal concerns a decision of the Kansas Supreme Court upholding § 4 of the Kansas Natural Gas Price Protection Act ("Kansas Price Protection Act"), Kan. Stat. Ann. ("K.S.A.") § 55-1404, which prohibits the operation of certain critical price adjustment provisions in long-term intrastate natural gas purchase contracts. The Kansas Supreme Court affirmed the trial court's rejection of

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[2] The federal constitutional issue in the first question presented herein was raised below in the trial court and the Kansas Supreme Court; both courts expressly rejected appellant's Contract Clause claim and upheld the constitutionality of the Kansas statute as applied in this case. See pp. 9-11, *infra*. Hence, an appeal lies pursuant to 28 U.S.C. § 1257(2). See *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234, 240 (1978); *United States Trust Co.* v. *New Jersey*, 431 U.S. 1 (1977).

The second question presented herein, involving the interpretation of a federal statute, may be considered on this appeal because once this Court has "appellate jurisdiction, [it] also take[s] jurisdiction over any aspects of the case which would otherwise fall solely within [its] certiorari jurisdiction." *Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 487 n.14 (1975) (and cases cited therein). If this Court should conclude that this entire case does not fall within its appellate jurisdiction, ERG requests that this statement be treated as a petition for a writ of certiorari, in which case jurisdiction would be invoked under 28 U.S.C. § 1257(3).

appellant's claim that the Kansas statute abridges Article I, Section 10, of the United States Constitution in that the legislation impairs the obligation of contracts and was passed at the instance of appellee, The Kansas Power & Light Co. ("KPL"), to permit that utility to avoid price increases otherwise lawfully mandated by its intrastate long-term purchase contracts with natural gas producers.[3]

Also involved in this appeal is the Kansas Supreme Court's rejection of ERG's claim that § 105(b)(1) of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3315(b)(1) (Supp. IV 1980), allowed a price increase under one of the escalator clauses in the contracts at issue. For its construction of this federal statute, the court below relied upon its earlier ruling in *Mesa Petroleum Co.* v. *The Kansas Power & Light Co.*, 229 Kan. 631, 629 P.2d 190 (1981), *petn. for cert. pending*, No. 81-711.

B. The Contracts.

ERG is a natural gas producer. It has two long-term gas purchase contracts with KPL, both entered into in 1975 and involving intrastate sales of natural gas. App. 3a.[4] Together, they commit to KPL all of ERG's natural gas production from the Spivey-Grabs field in Kansas for the entire life of the field or of the associated processing plants. *Id.* In exchange for this long-term supply commitment by ERG, KPL agreed that the pricing schedule in each contract would include identical provisions for upward price adjustment.

Accordingly, each contract contains, *inter alia*, two typical price adjustment provisions, which have been referred

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[3] This case may involve 28 U.S.C. § 2403(b). Appellant has served this jurisdictional statement on the Attorney General of Kansas.

[4] One of the contracts ("the Gas Purchase Contract") governs the sale of gas produced directly from the wells; the other ("the Residue Gas Contract") governs the sale of remaining gas after certain recovery and processing steps are completed. App. 3a. The relevant provisions of the contracts are included in the appendix accompanying this statement. App. 66a-70a.

to in this litigation as indefinite escalator clauses.[5] The first is a so-called "government pricing" provision.[6] It provides for escalation of the price to the highest level allowed by law for any vintage of gas produced in Kansas. The second indefinite escalator clause is a "price redetermination" clause.[7] It provides that upon request by ERG no more than once every two years, the parties must agree to a new price equal to the average of the three highest prices paid for natural gas in a stated geographical area and meeting certain specifications. In a separate section labelled "Intent", the contracts explain in no uncertain terms the purpose of these indefinite escalator clauses: "It is the intention of the parties that the price adjustment provisions contained herein are solely for the purpose of compensating SELLER for the anticipated increase in its operating costs and for the anticipated increase in the value of its Natural Gas to be sold hereunder."[8]

The contracts also make provision for termination at ERG's option if KPL refuses to accept a price increase occasioned by either of the indefinite escalator clauses. The so-called "Commission Approval" section of the con-

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[5] Indefinite price escalator clauses, which take various forms, generally call for the escalation of a contract price upon and according to the happening of specified contingencies not within the control of the parties to the contract. See generally *Pennzoil Co.* v. *FERC*, 645 F.2d 360, 366 & n.5 (5th Cir. 1981), *cert. denied*, No. 81-340 (Jan. 11, 1982); 4 H. Williams & C. Meyers, *Oil and Gas Law* § 726 (1981). To be distinguished are fixed or definite price escalator clauses, which provide for automatic, specified price increases at specified times.

[6] This provision is contained in § 6.7 of the Gas Purchased Contract and § 8.5 of the Gas Residue Contract. App. 66a.

[7] This provision is contained in § 7 of the Gas Purchase Contract and § 9 of the Residue Gas Contract. App. 67a-68a.

[8] This provision is contained in § 23 of the Gas Purchase Contract and § 25 of the Residue Gas Contract. App. 70a.

tracts[9] requires KPL to make application to the Kansas Corporation Commission ("KCC") for approval of any pass-through to consumers of increased costs arrived at under the price redetermination provision or the government pricing provision. If a pass-through is not approved, KPL may elect (but is not obligated) to pay the higher price. If KPL refuses to pay the increased price, ERG has the right to terminate the contract on 30 days' written notice.

C. The Statutes.

1. *The Natural Gas Policy Act.* The Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. § 3301 *et seq.* (Supp. IV 1980), was enacted on November 9, 1978, and took effect December 1, 1978. Before its enactment, prices charged by producers for intrastate sales of natural gas in Kansas were not regulated, while interstate gas sales were regulated under the federal Natural Gas Act of 1938, 15 U.S.C. § 717 *et seq.* (1976). A major purpose of Title I of the NGPA was to remedy the serious economic distortions perceived by Congress to have resulted from regulation under the Natural Gas Act, particularly the existence of dual interstate and intrastate markets. Congress' goal in Title I was to create a single national market, in part by imposing price controls during an interim period on interstate and intrastate sales of natural gas, leading to complete price deregulation of many categories of natural gas by January 1, 1985. See H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 67 (1978).

Title I contains an intricate set of price controls on various categories of natural gas in both the interstate and intrastate markets. Pertinent to this case are §§ 102 and 105 of that title, 15 U.S.C. §§ 3312, 3315. Section 102 sets a maximum price for sales of "new" natural gas, as

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[9] This provision is contained in § 8 of the Gas Purchase Contract and § 10 of the Residue Gas Contract. App. 69a.

that term is defined in the statute,[10] which price is adjusted upward monthly according to a formula set forth in § 102(b)(2).[11] Section 105 establishes a price ceiling for intrastate gas sales that were under contract on the date of enactment (November 9, 1978). Under § 105, the maximum lawful price for such intrastate sales is the lower of the price permitted by the terms of the contract as they existed on November 9, 1978, or the § 102 price for "new" natural gas.

2. *The Kansas Price Protection Act.* In response to enactment of the NGPA, ERG and other intrastate natural gas suppliers (whose contracts contained price adjustment clauses similar to ERG's government pricing provision) notified KPL that the price under those contracts would escalate to the NGPA § 102 level beginning December 1, 1978. KPL unsuccessfully petitioned the KCC for a pass-through of any increased price. App. 8a-10a. On February 16, 1979, Mesa Petroleum Company, one of KPL's intrastate suppliers, filed suit in Kansas state court seeking payment by KPL of the increased prices triggered by the NGPA or, in the alternative, termination of its long-term supply contract with KPL.

On April 25, 1979, almost six months after passage of the NGPA (but not long after the filing of Mesa's lawsuit), a bill (H.B. 2680) was introduced in the Kansas legislature at the end of its session to prohibit the operation of indefinite escalator clauses like the ones contained in the intrastate gas purchase contracts at issue here. KPL was the "main proponent" of H.B. 2680.[12] This bill,

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[10] The definition of "new" gas is in § 102(c), 15 U.S.C. § 3312(c). The gas involved in this litigation does not qualify as "new" gas.

[11] The formula takes into account an inflation adjustment factor, set forth in § 101 of the Act, 15 U.S.C. § 3311, and a "real growth" factor set forth in § 102(b)(2)(B), 15 U.S.C. § 3312(b)(2)(B).

[12] Special Comm. on Energy & Natural Resources, *Report on 1979 H.B. 2680—Restriction of the Operation of Indefinite Price Escalator Clauses in Certain Gas Purchase Contracts* (1979) ("Committee Report") (minority view) (App. 81a).

which became the Kansas Price Protection Act, was considered by a special joint committee of the two houses of the legislature on May 9-11 and May 14, 1979. On the latter date, the bill was approved by the special committee by a 17-15 vote and was passed by the Kansas House and Senate. The statute took effect upon publication on May 29, 1979. Section 4, K.S.A. § 55-1404, provides that

> "on or after December 1, 1978, the price allowed to be paid pursuant to federal legislation or any regulation by an agency implementing such legislation, or the price paid or to be paid for any sale of natural gas in the state of Kansas shall not be taken into account in applying any indefinite price escalator clause contained in any gas purchase contract subject to this act . . . ."

The limitation of § 4 terminates on December 31, 1984. K.S.A. § 55-1411.[13]

While the purported intent of the Kansas Price Protection Act is "to minimize the impact on consumers of natural gas price increases," [14] the reach of the statute is quite limited. It affects only intrastate natural gas purchase contracts entered into before April 20, 1977 and containing indefinite escalator clauses.[15] The statute thus does not apply even to all intrastate sales of natural gas in Kansas, which in 1978 involved only 15% of the gas produced in Kansas.[16] Only six percent of all natural gas produced in Kansas is subject to indefinite escalator

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[13] Certain statutory exceptions, contained in §§ 5 and 6, K.S.A. §§ 1405 & 1406, are discussed *infra* at 23 n.36.

[14] Committee Report 4 (App. 75a).

[15] Sections 3 & 4, K.S.A. §§ 55-1403 & 55-1404. Furthermore, even if they otherwise would be covered by §§ 3 and 4, contracts concerning stripper wells, new reservoirs, and new wells are exempted from coverage by § 6, K.S.A. § 55-1406.

[16] According to the Committee Report, of the 866.6 billion cubic feet ("Bcf") produced in Kansas in 1978, 731.6 Bcf were dedicated to the interstate market and 135 Bcf were sold intrastate. App. 73a.

clauses and therefore affected by the statute. Committee Report, *supra* note 12, at 3 (App. 73a). Even the bill's proponents expected merely that it "would provide a *modicum* of restraint on *some* utility price increases." *Id.* 4 (App. 75a) (emphasis added).

Moreover, § 8 of the statute, K.S.A. § 55-1408, authorizes contracting parties to "voluntar[ily] renegotiat[e] price provisions contained in [their] contracts," thereby delegating to private parties the right to circumvent the restriction otherwise imposed by § 4 of the Act. On the basis of considerations such as these and the haste with which the legislation was adopted, the minority report accompanying the bill stated that "the people of Kansas, especially the residential consumers, are the victims of a cruel hoax" in that the Act was "designed primarily to support the contention of KPL in its contract dispute with Mesa Petroleum Co., which is presently being litigated" in Kansas courts. Committee Report (minority view) 4 (App. 83a).

D. This Litigation.

1. *Background.* On November 9, 1978, the price under the contracts at issue here was $1.77 per Mcf. App. 6a. This was lower than the maximum price of $2.06 per MMBtu allowed by § 102 of the NGPA for that date.[17] Accordingly, on November 20, 1978 ERG notified KPL that by virtue of the government pricing provision of the contracts, the price would increase on December 1, 1978

[17] See 18 C.F.R. § 271.502(a) (1981). The term "Mcf" when used with respect to natural gas means 1,000 cubic feet of gas. The term is a measurement of volume. The term "MMBtu" when used with respect to natural gas means 1,000,000 British thermal units. MMBtu's measure energy. Typically, as a rule of thumb for gas measurement, one Mcf of gas may be taken to contain 1,000,000 British thermal units of energy; thus 1 Mcf equals approximately 1 MMBtu. For purposes of this litigation the terms "Mcf" and "MMBtu" may be used interchangeably. A price of $1.77 per Mcf thus is lower than a price of $2.06 per MMBtu.

to the then-applicable § 102 price of $2.078 per MMBtu. App. 7a. KPL refused to pay the increased price.[18] In June 1979, ERG notified KPL that the contracts were terminated. App. 10a. KPL denied that ERG had a right to terminate on the grounds that (1) the government pricing clause was not triggered by the NGPA, and (2) that the recently passed Kansas Price Protection Act prohibited the operation of the clause. App. 10a. On July 24, 1979, ERG requested price redetermination under that clause of the contracts. *Id.* KPL refused on the basis of the prohibition contained in the Kansas Price Protection Act. *Id.*

2. *Federal Questions Presented.* On July 2, 1979, ERG sought a declaratory judgment from the district court of Harper County that its termination of the two KPL contracts was proper. App. 10a. In its pleadings, ERG relied upon the NGPA as the basis for its entitlement to a price increase under the government pricing provision. *Id.* On August 20, 1979, ERG amended its pleadings to assert KPL's refusal to agree to an increase under the price redetermination clause as an additional ground for terminating the contracts. *Id.* In response to KPL's reliance on the Kansas Price Protection Act as a defense to both claims, ERG contended that the Kansas statute constituted an unlawful impairment of contractual obligations in violation of Article I, Section 10, of the United States Constitution. Both the statutory issue and the constitutional issue were briefed by the parties on cross-motions for summary judgment. *Id.*

3. *Federal Questions Considered and Resolved.* The trial court denied ERG's motion and granted KPL's cross-motion for summary judgment. It ruled that the

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[18] KPL petitioned the KCC on December 7, 1978 for a pass-through of the increased price, App. 8a, but the failure of the KCC to approve the pass-through within the period of time allowed by the contracts required KPL to elect to pay the increased price without any pass-through or risk termination of the contracts. App. 9a-10a.

government pricing clause was not triggered by the NGPA because the parties did not intend such legislation to trigger the clause. App. 27a-28a. ERG urged the court to avoid reaching the constitutionality of the Kansas Price Protection Act by construing the statute to allow ERG to terminate the contracts if the escalation provisions could not operate. The court concluded, however, that it was "unable to resolve this controversy in a manner that avoids the constitutional issue." App. 34a. It upheld the Act's constitutionality and concluded that, because of that statute, ERG could neither raise its price pursuant to the price redetermination clause nor terminate its contracts with KPL. App. 34a-41a. Relying exclusively upon the majority committee report accompanying the legislation and failing to acknowledge the limited reach of the statute (see pp. 7-8, *supra*), the trial court sustained the Act's constitutionality by finding that it was a reasonable measure with a "legitimate public purpose," App. 37a, in that it would serve to protect "consumers, already buffeted by rapidly increasing inflation, including spiraling utility costs . . . ." *Id.*

The Kansas Supreme Court affirmed. It disagreed with the trial court's rationale as to why the government pricing provision was not triggered by the NGPA. The court held that "the parties *intended* that the government price escalation clauses be triggered by enactments such as the NGPA." App. 14a (emphasis in original). But the court interpreted § 105(b)(1) of the NGPA in a way that precluded escalation under the government pricing clause, relying on its previous decision in *Mesa Petroleum Co.* v. *The Kansas Power & Light Co.*, 229 Kan. 631, 629 P.2d 190 (1981), *petn. for cert. pending*, No. 81-711, whose rationale the court found to be "fully applicable here." App. 14a-15a.[19]

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[19] The rationale of the Kansas Supreme Court in *Mesa Petroleum* was that § 105(b)(1) sets a ceiling price of the lower of the § 102 price for a given month or "the price under the terms of the existing contract, to which such natural gas was subject on November 9,

The court then considered the effect of the Kansas Price Protection Act on the price redetermination clause, App. 15a, and affirmed the trial court's decision upholding the Kansas statute.[20] App. 15a-22a. As had the trial court, the Supreme Court concluded that the issue could not be resolved "in a manner which would avoid the constitutional issue," App. 16a, and held that ERG could neither raise its price under the price redetermination clause nor terminate the contracts. App. 34a. The court adopted verbatim the reasoning of the trial court on the constitutional question. App. 16a-22a.

THE QUESTIONS ARE SUBSTANTIAL

The principal question presented herein involves the constitutionality of § 4 of the Kansas Price Protection Act. ERG contends that the constitutional analysis applied below to sustain the validity of that statute conflicts squarely with the Contract Clause analysis consistently articulated by this Court, in that the Kansas courts uncritically supposed a legitimate purpose on the part of the Kansas legislature even though such a purpose clearly was belied by the statute's plain terms, impact, and legislative history. Each of these demonstrates that the hastily adopted Kansas Price Protection Act was designed to relieve KPL, one of the state's largest utilities, of obligations it had incurred pursuant to many otherwise valid long-term natural gas purchase contracts,

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1978"; that the latter phrase means the "contract price" on November 9; that the contract price under these contracts on November 9, 1978 was lower than the § 102 price; and therefore that the price does not escalate.

[20] The court did not separately consider the effect of the Kansas statute on the government pricing provision because it ruled that escalation under that provision was barred in any event by § 105(b)(1) of the NGPA. See p. 10 & n.19, *supra*. The court did not limit its rationale, however, to the statute's application to the price redetermination clause, but discussed and sustained the constitutionality of the statute's prohibition of indefinite escalator clauses generally.

while affecting the price of only a fraction of the natural gas sold in Kansas.

If generally applied, the Kansas Supreme Court's reasoning would permit States to enact special legislation designed to relieve powerful private constituencies of significant contractual obligations on the basis of unfounded and broad assertions of the public benefits to be derived from the enactment, with utter indifference to the legitimate interests of the other contracting parties. If such legislation is allowed to be sustained, then the Contract Clause indeed is, contrary to what this Court has said, a "dead letter." [21] This case self-evidently presents substantial questions worthy of this Court's plenary consideration.

The second question presented, whether § 105(b)(1) of the NGPA allowed ERG to escalate prices pursuant to the government pricing clause, is identical to the question presented in *Mesa Petroleum*, which this Court has before it for consideration in No. 81-711. As is shown herein, in the *Mesa Petroleum* petition, and in the Brief for the United States and the Federal Energy Regulatory Commission, as *amici curiae* (urging summary reversal in *Mesa Petroleum*), the Kansas Supreme Court's construction of § 105(b)(1) is in conflict with that of the Federal Energy Regulatory Commission and the Court of Appeals for the Fifth Circuit, as well as the plain terms and legislative history of the statute.[22]

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[21] *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234, 241 (1978).

[22] The constitutional question presented herein cannot be avoided by resolution of the statutory question. This is because the Kansas Supreme Court's ruling on § 105(b)(1) of the NGPA affects only the government pricing provision of the contracts, not the wholly independent price redetermination provision. The Kansas Supreme Court found that it could not deny ERG's claim under the latter contract provision without relying on the Kansas Price Protection Act and upholding its constitutionality.

Moreover, if this Court reverses the Kansas Supreme Court on § 105(b)(1)—either in this case or in *Mesa Petroleum*—the Kansas

A. The Kansas Price Protection Act Works a Substantial Impairment of the Obligation of Contracts in a Manner Violative of Article I, Section 10, of the United States Constitution.

The Contract Clause provides that "No state shall . . . pass any . . . Law impairing the Obligation of Contracts . . . ." While "the prohibition is not an absolute one and is not to be read with literal exactness",[22] it does impose restraints on the authority of a State "to abridge existing contractual relationships, even in the exercise of its otherwise legitimate police power." *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234, 242 (1978); see *id.* at 244. Indeed, in its two most recent Contract Clause decisions, this Court reaffirmed the vitality of the Clause and struck down state laws less objectionable than the legislation here. See *Allied Structural Steel, supra; United States Trust Co.* v. *New Jersey*, 431 U.S. 1 (1977). The decision below conflicts with this Court's recent decisions interpreting the Contract Clause and with the Court's earlier precedent, including the leading case of *Home Building & Loan Association* v. *Blaisdell*, 290 U.S. 398 (1934).

1. *The Kansas Price Protection Act works a severe, substantial impairment of contractual obligations.*

In Contract Clause analysis, "the first inquiry must be whether the state law has, in fact, operated as a substantial impairment of a contractual relationship." *Allied Structural Steel*, 438 U.S. at 244. It is clear that there was such an impairment here. The Price Protection Act renders invalid the central term of these long-

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courts undoubtedly would apply the Price Protection Act to bar escalation under the government pricing provision. *Cf.* note 20 *supra*. The issue of the constitutionality of the Kansas statute has not been presented to this Court in the petition for certiorari in *Mesa Petroleum*, and must therefore be resolved in the instant case.

[22] *Home Building & Loan Ass'n* v. *Blaisdell*, 290 U.S. 398, 428 (1934).

term purchase contracts—the price term. This was not a "minimal contractual interest," as the trial court thought. App. 36a. Nor is the legislative modification a "relatively inconsequential infringement of contract rights," *United States Trust*, 431 U.S. at 44 (Brennan, J., dissenting); it goes to the very "heart of the obligation." *Id.* at 41. And unlike the situation in *Blaisdell*, where contractual benefits were merely postponed, or in *City of El Paso* v. *Simmons*, 379 U.S. 497 (1965), where enforcement remedies were altered, here ERG's right to the contract price for all gas supplied between December 1, 1978 and December 31, 1984 is "irretrievably lost." *Sonoma County Organization of Public Employees* v. *County of Sonoma*, 591 P.2d 1, 7, 152 Cal. Rptr. 903 (1979) (*en banc*).

Nor is it true, as the courts below maintained, that the Kansas statute merely prevents ERG from "reap-[ing] unanticipated, windfall financial benefits." App. 18a, 36a (quoting Committee Report 4 (App. 74a)). ERG relied heavily on the inclusion of provisions for price escalation when it agreed to commit all of its gas production from the Spivey-Grabs field to KPL over the entire life of the field and its associated processing plant. It has long been recognized that this kind of contract to sell a scarce and increasingly valuable commodity over a long term is exceptionally favorable to the buyer and unfair to the seller unless provision is made for increasing the contract price to keep pace with the market.[24] KPL's agreement to pay the price required by the contract was KPL's "central undertaking" and was "the primary consideration for [ERG's] undertaking." *City of El Paso*, 379 U.S. at 514. ERG "was substantially induced to enter into these contracts on the basis of"

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[24] E. Neuner, *The Natural Gas Industry* 265-66 (1960). This is particularly true with respect to a buyer like KPL, which for business reasons must establish long-term commitments for natural gas. *Id.*; see *Superior Oil Co.* v. *Western Slope Gas Co.*, 604 F.2d 1281, 1287 n.8 (10th Cir. 1979); 4 H. Williams & C. Meyers, *Oil and Gas Law* § 726, at 748.4-748.5 (1981).

KPL's promise to pay the price called for by the contract —including its escalation provisions. *Id.* Thus, the Kansas statute is not an unassailable law "which restrict[s] a party to those gains reasonably to be expected from the contract", *id.* at 515; on the contrary, it deprives ERG of its reasonably expected gains and gives a substantial windfall to KPL.[25]

In short, ERG would not have entered into these long-term contracts, under which it committed a substantial amount of its natural gas for a long period of time, without the assurance that it would be compensated for future increases in the value of its product. Obliteration of this right constituted a substantial, severe impairment of these contracts.

2. The impairment does not further an important public purpose and, in any event, would be an unnecessary and unreasonable means even to a legitimate end.

In considering whether a state's impairment of contractual obligations is constitutional, the "height of the hurdle the state legislation must clear" is determined by

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[25] The centrality of the escalation clauses to the parties' reciprocal undertakings, and the extent of ERG's reliance on these clauses, is demonstrated further by the intent, termination, and government regulation provisions of the contracts. The parties specifically expressed their intent that the *sole* purpose of the price escalation provisions was to "compensat[e] [ERG] for the anticipated increase in its operating costs and for the anticipated increase in the value of its Natural Gas to be sold" under the contracts. App. 70a. ERG specifically identified changes in government regulation as one of the eventualities that could trigger a price increase. App. 66a. Further, ERG anticipated that KPL might refuse to pay increased prices if it could not pass them on to its customers, and therefore preserved for itself the option to terminate the contracts in that event. App. 69a. Finally, while the parties agreed (in § 18 of the Gas Purchase Contract and § 20 of the Residue Gas Contract) that the contracts would be subject to present and future laws, they made clear that this agreement would *not* affect, among other things, ERG's right to terminate the contracts if it could not receive the benefit of its bargain in the form of the enumerated price increases. App. 69a-70a.

the degree of impairment. *Allied Structural Steel*, 438 U.S. at 245. Severe impairment, as in this case, "will push the inquiry to a careful examination of the nature and purpose of the state legislation." *Id.* Since *Blaisdell*, this Court's examination has focused on the five factors considered significant by the *Blaisdell* Court,[26] whose opinion "clearly implied that if the Minnesota moratorium legislation [upheld in *Blaisdell*] had not possessed the characteristics attributed to it by the Court, it would have been invalid under the Contract Clause of the Constitution." *Id.* at 243.

Rather than engage in careful scrutiny of the Kansas statute, the court below simply deferred to the legislature's judgment as to the "reasonableness" of the Price Protection Act. App. 18a, 36a. Indeed, the Kansas Supreme Court adopted verbatim the statements of the trial court, App. 16a-22a, which itself had adopted verbatim the statements of the majority of the special committee that recommended the legislation. App. 34a-40a. No consideration was given to the fact that the reach of the statute falls far short of the broad benefits attributed to it. Nor did the Kansas courts acknowledge the strong opposition to the legislation, on grounds highly relevant to Contract Clause analysis, by nearly half of the special committee that considered it. The Kansas Price Protection Act cannot survive the careful examination mandated by this Court.

(a) *The impairment does not further an important general social purpose.*

In determining whether the end sought to be achieved by the state legislature justifies the impairment of a

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[26] "First, the state legislature had declared in the Act itself that an emergency need for the protection of homeowners existed. [290 U.S.,] at 444. Second, the state law was enacted to protect a basic societal interest, not a favored group. *Id.*, at 445. Third, the relief was appropriately tailored to the emergency that it was designed to meet. *Ibid.* Fourth, the imposed conditions were reasonable. *Id.*, at 445-447. And, finally, the legislation was limited to the duration of the emergency. *Id.*, at 447." *Allied Structural Steel*, 438 U.S. at 242.

contractual obligation, this Court has focused on two criteria: first, whether the legislation was enacted because of an "emergency"; and second, whether the legislation "was addressed to a legitimate end," that is, whether it was "for the mere advantage of particular individuals [or] for the protection of a basic interest of society." *Blaisdell*, 290 U.S. at 444-45; see *id.* at 420-29; *Allied Structural Steel*, 438 U.S. at 242.

Here, there was no emergency. No such finding was or could have been made by the Kansas legislature. The increasing cost of energy is not a new problem, and Kansas had never before regulated prices charged by producers in intrastate sales of natural gas.[27] Enactment of the NGPA was a new development, but if it had caused a true emergency within the meaning of *Blaisdell*, the Price Protection Act should have been at the forefront of the Kansas legislature's consideration when the 1979 session opened in January, more than two months after passage of the NGPA. Instead, the legislation was not proposed until only twenty days remained in the legislature's five-month session, and then only after KPL found itself in court with Mesa Petroleum over KPL's refusal to pay increased prices required by its contracts.

Furthermore, while the Kansas legislature sought to avert some of the consequences flowing from the NGPA's phased deregulation of natural gas, Congress viewed that very deregulation and the consequential increase in prices as ultimately in the public interest. While differences may exist as to preferable policy,[28] an objective

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[27] The presence or absence of previous state regulation has been identified by this Court as a factor to be considered in assessing the constitutionality of a legislative impairment of contractual rights. Compare *Allied Structural Steel*, 438 U.S. at 242 n.13, 249, with *Veix* v. *Sixth Ward Building & Loan Ass'n*, 310 U.S. 32, 38 (1940).

[28] To be sure, in § 602 of the NGPA, 15 U.S.C. § 3432, Congress ceded to the States the authority to establish maximum lawful prices lower than those prescribed in the NGPA, but this is not

situation considered beneficial to the public by Congress cannot at the same time be deemed an "emergency" justifying the impairment of valid contracts. "This legislation, [causing] a sudden, totally unanticipated, and substantial retroactive [change in the contracts] was not enacted to deal with a situation remotely approaching the broad and desperate emergency economic conditions of the early 1930's—conditions of which the Court in *Blaisdell* took judicial notice." *Allied Structural Steel*, 438 U.S. at 249. The Kansas Supreme Court's perception of an "emergency situation," App. 22a, must be regarded "as lacking in adequate basis." *Blaisdell*, 290 U.S. at 444.

Nor was the Price Protection Act "addressed to a legitimate end" by furthering "an important general social problem." *Allied Structural Steel*, 438 U.S. at 247; see *id.* at 242; *Blaisdell*, 290 U.S. at 445. While the Kansas Supreme Court credited the legislature with supposed concern for the effect on consumers of inflation and rising utility costs, App. 18a-19a, 22a, even the bill's proponents expected only that it "would provide a *modicum* of restraint on *some* utility price increases." Committee Report 4 (App. 75a) (emphasis added). Facts that were before both the legislature and the Kansas Supreme Court confirm the limited impact of the statute on the problems it supposedly addresses. First, only 15% of the natural gas produced in Kansas is sold intrastate, Committee Report 3 (App. 73a), and only a fraction of the gas consumed in Kansas is derived from intrastate sales.[29] Second, the statute affects indefinite, but not

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what the Kansas legislature has done. As we show in detail below, rather than impose price ceilings on intrastate sales, in what would have been a sharp departure from Kansas' prior policy, the Kansas legislature decided only to prohibit certain kinds of escalator clauses in certain contracts—but even then subject to an exception for voluntary agreement by the contracting parties—while leaving most of the intrastate natural gas market wholly unregulated. See pp. 7-8, *supra*, and 18-19, *infra*.

[29] Statistics prepared for the Kansas legislature show that 71% of the residential and commercial requirements for natural gas in

fixed, escalator clauses; the former are found in contracts covering only six percent of the natural gas produced in Kansas. *Id.* Third, the statute exempts some of the natural gas contracts that otherwise would be within even the limited coverage of the statute. See note 16, *supra*. Thus, the price of most of the natural gas produced or used in Kansas is unaffected by the Price Protection Act.[30]

On the other hand, KPL had a great stake in the passage of the Kansas Price Protection Act and, accordingly, was its "main proponent." Committee Report (minority view) 2 (App. 81a). One-third of KPL's natural gas purchase contracts contain indefinite escalator clauses like the ones in the ERG contracts.[31] The minority report went so far as to say that the "people of Kansas, especially the residential consumers, are the victims of

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Kansas were served by the Cities Service Gas Company, an *interstate* natural gas pipeline company whose contracts therefore are not affected by the Price Protection Act. Cities Service also provides 49% of the natural gas used for the generation of electrical power and industrial and other uses. Kansas Legislative Research Department, *The Effect of the Natural Gas Policy Act (NGPA) of 1978 on Kansas* 3 (March 27, 1979). Consumption of natural gas in Kansas totalled 566.6 Bcf in 1975; even assuming that consumption did not increase at all between 1975 and 1978, the figures before the legislature would have shown that at most 23.8% of the total consumption was provided by intrastate sales. Committee Report 3 (App. 73a).

[30] The Kansas statute was copied from a similar statute enacted earlier in 1979 in Oklahoma "to fit Oklahoma circumstances" which were entirely different from those in Kansas. Committee Report (minority view) 3, 4 (App. 82a, 84a). The percentage of sales affected by indefinite escalator clauses in Oklahoma is significantly higher than in Kansas. *Id.*

[31] KPL is not a particularly appropriate representative of consumer interests: It sells "approximately 69 percent of its gas to industrial customers, other utilities, and to itself for use in the generation of electricity," not to residential consumers, and uses much of the gas as boiler fuel, which is an "inappropriate and inefficient use." Committee Report (minority view) 2 (App. 82a).

a cruel hoax," for it appeared that the bill was "designed primarily to support the contention of KPL in its contract dispute with Mesa Petroleum Co., which is presently being litigated in Grant County District Court. The Legislature should not become involved by taking sides in such contract disputes." *Id.* 11.[32]

This is, in short, the very kind of special legislation that the Contract Clause is supposed to prevent, in which the State has "adopt[ed] as its policy" the repudiation of one party's contractual obligations to another. *Blaisdell*, 290 U.S. at 439; see *Allied Structural Steel*, 438 U.S. at 256 (Brennan, J., dissenting). KPL may not have been the only utility to benefit from the prohibition of indefinite escalator clauses, "[b]ut whether or not the legislation was aimed largely at a single [company], it clearly has an extremely narrow focus." *Allied Structural Steel*, 438 U.S. at 248. "[T]his law can hardly be characterized, like the law at issue in the *Blaisdell* case, as one enacted to protect a broad societal interest rather than a narrow class." *Id.* at 248-49. Since there has been no showing that "this severe disruption of contractual expectations was necessary to meet an important general social problem[,] [t]he presumption favoring 'legislative judgment as to the necessity and reasonableness of a particular measure,' *United States Trust Co.*, 431 U.S. at 23, simply cannot stand in this case." *Allied Structural Steel*, 438 U.S. at 247. Indeed, this Court need not even consider whether the means chosen by the legislature were reasonable, since the end served by the statute is not legitimate.[33]

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[32] While legislative motive is often not relevant in other contexts, "'[i]t is the motive, the policy, the object, that must characterize the legislative act, to affect it with the imputation of violating the obligation of contracts.'" *City of El Paso*, 379 U.S. at 509 (quoting *Ogden* v. *Saunders*, 25 U.S. (12 Wheat.) 213, 291 (1827)).

[33] See *Sonoma County Organization of Public Employees* v. *County of Sonoma*, 591 P.2d 1, 10, 152 Cal. Rptr. 903 (1979) (*en banc*).

(b) *The means adopted were not reasonable or necessary to serve an important public purpose.*

Even assuming that the legislature's aim was to protect consumers from the inflationary effects of increased natural gas prices, App. 18a-20a, 36a-38a, and assuming further that this is a "vital" public interest, *Blaisdell*, 290 U.S. at 439, the constitutional inquiry is not at an end. The fact that a legislature's goals are "important and of legitimate public concern" is not an invitation to the courts "to engage in a utilitarian comparison of public benefit and private loss." *United States Trust*, 431 U.S. at 28-29. Contrary to the impression of the courts below, App. 17a, 35a, this Court "has not 'balanc[ed] away' the limitation on state action imposed by the Contract Clause." 431 U.S. at 29 (quoting *City of El Paso*, 379 U.S. at 517 (Black, J., dissenting)). "Despite the customary deference courts give to state laws directed to social and economic problems," *Allied Structural Steel*, 438 U.S. at 244, legislation modifying contractual rights and obligations must use means that are (1) "necessary" to serve the "important public purpose" and (2) "reasonable" in their terms and conditions. *United States Trust*, 431 U.S. at 25.

1. As in *United States Trust*, "[t]he determination of necessity can be considered on two levels." 431 U.S. at 29. First, as construed by the courts below, the statute effected a more "drastic" modification of these contracts than was necessary. *Id.* at 30. It was unnecessary to deprive ERG not only of its contractual right to escalation but also of its alternative right to terminate the contracts; at least ERG should be allowed to sell its gas elsewhere, unless the primary aim of the legislation is, as we have suggested, protection of KPL.[34]

[34] The Kansas legislature and even KPL assumed that one of the results of enactment of the Price Protection Act might be the cancellation of intrastate contracts containing indefinite escalator clauses and a consequent redirection of natural gas resources into the henceforth more profitable interstate market. See Committee

Second, "without modifying the [contract] at all, the State[] could have adopted alternative means of achieving [its] goal[]" of protecting consumers from price increases. *Id.* at 29-30. The KCC, after all, has authority to protect the interests of Kansas energy consumers; by denying KPL a pass-through of its increased costs, it could achieve the goal of consumer protection. Indeed, the legislature could have asserted its own authority (otherwise delegated to the KCC) to prohibit the pass-through of increased costs to consumers.[35] The legislature created a false dichotomy in thinking it had to side with either producers or consumers in this instance: It is obvious that neither should bear the burden assumed by KPL when it executed these and like contracts; KPL agreed to certain terms and should have to live with them.

2. The Kansas Price Protection Act is far from a reasonable measure for accomplishing the legislature's stated goal. Its limited scope and abundant exemptions ensure that it could not even begin to solve the problem of rising utility costs. While the court below found in the statute's exceptions a measure of reasonableness and tailoring, App. 20a-21a, it is the statute's arbitrary selectivity and under-inclusiveness that reinforces the conclusion of invalidity.

For example, the statute does not apply to any *fixed* escalation clauses, even though such clauses can lead to

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Report 4 (App. 75a); (minority view) 3 (App. 83a). Such an interpretation of the statute would have made its impact less harsh while effectuating the legislature's legitimate aims. *Cf. E & E Hauling, Inc.* v. *Forest Preserve District*, 613 F.2d 675, 679-80 (7th Cir. 1980) (when damages may be awarded for breach of contract, there is no unconstitutional impairment of contract). But the Kansas Supreme Court interpreted the statute not to allow termination or an award of damages, thus making the statute even more onerous than its terms required.

[35] Alternatively, the legislature could have set maximum prices for all natural gas, thereby protecting the consumers generally from price increases.

prices as high as the ceiling set by NGPA § 102. The statute does not apply at all to contracts executed after April 20, 1977, even though they may contain fixed or indefinite escalator clauses permitting increases up to the § 102 level. Most objectionable—and telling—is the statute's allowance of *voluntary* renegotiation of prices even in contracts otherwise covered by the statute, including the ones here at issue. This exemption enables KPL to exact concessions from ERG and other natural gas producers in exchange for KPL's agreement to allow the contracted-for price escalation. While the court below thought this allowance of voluntary negotiations for new contractual price provisions "guarantee[s] a measure of fairness," App. 21a, it hardly is fair to transform a contract obligation into what one party to the contract may be willing to renegotiate.

On the other hand, the statute's effect on *these contracts* (and others like them) is not tempered by statutory conditions as was the case in *Blaisdell*. There, mortgagees' rights to foreclose were postponed during the duration of an emergency, but the conditions upon which the period of redemption was extended were found reasonable because they preserved to the mortgagee the greater part of its rights under the mortgage. 290 U.S. at 445. Here, the impairment is not so tempered.[36]

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[36] Section 5 of the Kansas Price Protection Act does allow the escalation of prices to a ceiling specified in § 109 of the NGPA for gas (unlike that at issue here) not otherwise covered by the federal statute. The § 109 price is, however, so much lower than the § 102 price (to which ERG would be entitled but for the Kansas statute) that until April, 1980, the § 109 price was *lower* than the price specified in the contracts at issue even without any escalation under the two indefinite escalator clauses. See 18 C.F.R. §§ 271.902, 271.101(a) (Table 1) (1981). Moreover, KPL has maintained in separate litigation that under § 5 of the Kansas statute ERG was not entitled to the § 109 price until November, 1981, and even after that date was not entitled to the full § 109 price. *The Kansas Power & Light Co.* v. *Energy Reserves Group, Inc.*, No. 81-C-13 (Harper County, Kansas District Court). There is another exemp-

Similarly, the statute's prohibition is unreasonable in that it lacks the temporary character found so important in *Blaisdell*. 290 U.S. at 440, 445; see *Allied Structural Steel*, 438 U.S. at 242. The court below saw virtue in the fact that the Kansas statute expires on December 31, 1984, App. 20a, but that fact is not relevant. In *Blaisdell*, the *impairment* was temporary because effectuation of the mortgagee's enforcement rights was merely postponed. Here, on the other hand, the statute's effect is permanent and irrevocable. ERG is required to sell its gas to KPL at a price far below market value for the period from December 1, 1978, through December 31, 1984. ERG will never recoup these losses. The statute's life may terminate at the end of 1984, but the impairment is permanent.

3. In short, this is a case where the state legislature has acted "[w]ith studied indifference to the interests of the [natural gas producer] or to his appropriate protection." *W.B. Worthen Co.* v. *Kavanaugh*, 295 U.S. 56, 60 (1935). The indifference is evident not only from the statute's nature, purpose, and effect, but also from the method of its adoption. The Committee minority voiced "strenuous objection to the procedure employed by the proponents during the Committee deliberation." Committee Report (minority view) 4 (App. 84a). In particular, "[t]he parliamentary tactics used effectively precluded the presentation and debate of a number of amendments which . . . are needed if legislation such as H.B. 2680 is to be passed . . . . It is evident from the fact that 15 of the members opposed the Committee recommendation that the Committee should have devoted more of its efforts

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tion in § 6 of the Price Protection Act for stripper well gas, but it has, since November, 1981 afforded ERG price relief on only 7% of the gas at issue. In short, then, § 4 of the Kansas Price Protection Act stands as an overwhelming barrier to ERG's recovery of anything approaching the price to which it is entitled under the contracts at issue.

to debate and discussion of the specific provisions of the bill." *Id.*

In sum, just as the state legislators in *Kavanaugh* took from a mortgagee "the quality of an acceptable investment for a rational investor," 295 U.S. at 60, those here have taken from ERG the quality of an acceptable commercial transaction for a rational businessman. "So viewed [the state legislation is] seen to be an oppressive and unnecessary destruction of nearly all the incidents that give attractiveness and value" to the contracts here at issue. *Id.* at 62; see *United States Trust*, 431 U.S. at 56 (Brennan, J., dissenting). It cannot be sustained.[37]

B. The Decision Below Misinterprets Section 105(b)(1) of the Natural Gas Policy Act, and Conflicts with the Interpretation of the Fifth Circuit and the Federal Energy Regulatory Commission.

Pursuant to § 105(a) of the NGPA, the maximum lawful price for sales under intrastate contracts that were

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[37] Resolution of the constitutional question is important because of its practical impact on the many natural gas producers and pipeline companies who are parties to contracts containing indefinite escalator clauses. In the preamble to its final regulations under the NGPA, the Federal Energy Regulatory Commission discussed the need for clear guidance in the related area of the effect of the federal statute on indefinite escalator clauses and expressed its awareness "that continued uncertainty with respect to the contractual rights of the parties could (and would if allowed to go on much longer) have serious detrimental effects in the marketplace." 44 Fed. Reg. 16895, 16896 (Mar. 20, 1979).

This Court's resolution of the Contract Clause question also would give needed guidance to several lower state and federal courts now faced with this question in connection with the Kansas statute and the similar Oklahoma statute (see note 30 *supra*). See, *e.g.*, *Edmiston* v. *State Corporation Commission*, No. 79-1335 (D. Kan. Nov. 24, 1980) (rejecting Contract Clause challenge), *as modified* (D. Kan. Jan. 13, 1981), *appeal docketed*, No. 81-1197 (10th Cir. Feb. 23, 1981); *Energy Consumers & Producers Ass'n* v. *Baker*, No. 79-320-D (W.D. Okla., filed Mar. 20, 1979); *Oklahoma Independent Petroleum Ass'n* v. *Baker*, No. 79-823-D (W.D. Okla., filed July 20, 1979) (consolidated with No. 79-320-D).

in existence on the date of the NGPA's enactment (November 9, 1978) is set by § 105(b). Section 105(b) establishes two different price ceilings for intrastate contracts. The applicable ceiling is determined by the contract price on November 9, 1978. If the contract price on November 9 was *lower* than the ceiling price for that date set by § 102 of the NGPA for "new" gas, then the maximum lawful price thereafter is governed by § 105(b)(1). If on November 9, 1978, the contract price was *higher* than the § 102 price, then § 105(b)(2) governs. Under the contracts in question, the price on November 9 was $1.77 per Mcf, which was *lower* than the § 102 price for that date ($2.06 per MMBtu). Paragraph (b)(1) of § 105 therefore governs here, and paragraph (b)(2) has no application.

Under § 105(b)(1), the maximum price for sales in any month is the lower of "the price under the terms of the existing contract, to which such natural gas was subject on November 9, 1978, as such contract was in effect on such date" (§ 105(b)(1)(A)) or the maximum lawful price for that month for new gas under § 102 (§ 105(b)(1)(B)). It has been ERG's contention that under the contracts here at issue, the "price under the terms of the existing contract" by definition was and always will be equal to the maximum lawful price under § 102. This is because "under the terms of the existing [ERG-KPL] contract," the government pricing escalator clause, as construed by the court below, App. 12a, calls for automatic escalation to the § 102 price.

The court below, however, misconstrued § 105(b)(1) to preclude escalation. Applying its earlier holding in the *Mesa Petroleum* case, the court read the § 105(b)(1)(A) reference to "the price under the terms of the existing contract" on November 9, 1978, to mean the "contract price on November 9, 1978," which was lower than the § 102 price on that date. It therefore concluded that the November 9, 1978 price was the maximum price for these contracts. Thus, the court held "that under the terms of the government price escalator clause in these

contracts, and under the applicable section of the NGPA, *the November 9th gas price* (which was lower than the Section 102 price) did not escalate." App. 14a-15a (emphasis added).

The Kansas Supreme Court's construction of § 105 (b) (1) effectively reads that provision out of the statute. Section 105(b) (1) comes into play only if the contract price on November 9, 1978 is lower than the § 102 price. By reading § 105(b) (1) (A)'s reference to the "price under the terms of the contract" as of November 9 to mean the November 9 "contract price," the Kansas Supreme Court has immutably fixed the November 9 price as the § 105(b) (1) price because it *always* will be lower than the constantly increasing § 102 price. See pp. 5-6, *supra*.[38] This reading entirely defeats Congress' purpose, specifically expressed in the Conference Committee Report, to give effect to pre-existing escalation clauses as long as the escalated price would not exceed the § 102 price.[39] Under the Kansas court's analysis, § 105(b) (1),

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[38] Had Congress intended to focus on the November 9 contract price, it could have said so in clear terms. Indeed, this is what Congress did in § 105(b)(2). That section governs when the contract price on November 9 is *higher* than the § 102 price for that date, and dictates that the maximum lawful price in a given month is the higher of the § 102 price for that month or *"the contract price on November 9, 1978"* multiplied by an inflation factor for subsequent months. As the Chairman of the House Subcommittee that reported out the NGPA explained, "The phrase 'the price under the terms of the . . . contract' used in section 105(b)(1) *refers to the contract schedule of prices or contract mechanism for establishing prices over time.*" 124 Cong. Rec. H13117 (daily ed. Oct. 14, 1978) (emphasis added). That phrase "must be distinguished from the phrase 'contract price' used in section 105(b)(2). The latter is date specific, referring to the price paid under the contract for gas deliveries on date of enactment." *Id.*

[39] The Report explains:

> "If the contract price in effect on the date of enactment is less than the new gas ceiling price, the maximum lawful price for any subsequent month is the lower of (1) the price under the terms of the existing contract in effect on the date of enactment, or (2) the new gas price. *Thus, the price under the*

which was specifically written to permit escalation according to contract terms such as these, will never operate.[40]

For these reasons, both the Federal Energy Regulatory Commission ("FERC")[41] and the United States Court of Appeals for the Fifth Circuit[42] have interpreted

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contract may escalate through the operation of both fixed price escalator clauses and indefinite price escalator clauses in existence as of the date of enactment, but the price may not exceed the new gas price." H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 82 (1978) (emphasis added). See also 124 Cong. Rec. H13117 (daily ed. Oct. 14, 1978) (remarks of Rep. Dingell).

[40] Not allowing intrastate gas prices to escalate to the applicable NGPA price would undermine Congress' goal of encouraging the development of natural gas supplies by means of price incentives in order to lessen the potential for even greater price increases in the future. See p. 5, *supra*.

[41] After some initial confusion in which FERC, like the court below, used the term "contract price" interchangeably with the term "price under the terms of the existing contract," FERC changed its regulations to track the statutory language. See 18 C.F.R. § 271.502(a) (1981). FERC explained that the change was responsive to comments that pointed out that this incorrect use of the term "contract price" would prohibit the operation of fixed and indefinite escalator clauses in contracts whose November 9 contract price was lower than the § 102 price on that date. FERC changed the regulation because it agreed with the commenters that this would be more restrictive than the statute. In making the change, FERC sought to "allay the apprehension of those commentors who feared that fixed or indefinite price escalator clauses in contracts were abrogated by § 271.502(a)(1)." 43 Fed. Reg. 56448, 56475 (Dec. 1, 1978).

[42] The Court of Appeals for the Fifth Circuit has interpreted § 105(b)(1) to provide that "the maximum lawful price is the lower of the Section 102 price or the current price under the existing intrastate contract (*rather than the November 9th price*)." *Pennzoil Co.* v. *FERC*, 645 F.2d 360, 376, *cert. denied*, No. 81-340 (Jan. 11, 1982) (emphasis added). The court elaborated:

> "If . . . the price on November 9th was less than section 102, under section 105(b)(1) the maximum lawful price is the *current price provided for under the terms of the contract* as long as it does not exceed the section 102 price. . . .
>
> "Congress thus codified intrastate prices existing on November 9th if higher than section 102, but codified the 'contract

§ 105(b)(1) as we here urge. Indeed, the United States and the Federal Energy Regulatory Commission have urged this Court to reverse summarily the Kansas Supreme Court's identical statutory holding in *Mesa Petroleum*, which was found to be "fully applicable here." App. 14a-15a.

CONCLUSION

For the foregoing reasons, this Court should note probable jurisdiction and set this case for plenary review.

Respectfully submitted,

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January 21, 1982

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schedule of prices or contract mechanism for establishing prices *over time*' subject to the cap of section 102 if the November 9th price was less than section 102. 124 Cong. Rec. H13117 (daily ed. Oct. 14, 1978) (statement of Rep. Dingell) (emphasis in original)." *Id.* at 374-75 (first emphasis added).

Appendix

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No. 81-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY, INC.,
Appellee.

On Appeal from the Supreme Court of Kansas

APPENDIX TO JURISDICTIONAL STATEMENT

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APPENDIX A

SUPREME COURT OF KANSAS

No. 52,677

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

KANSAS POWER AND LIGHT COMPANY,
Appellee.

SYLLABUS BY THE COURT

1. OIL AND GAS—*Gas Purchase Contract—Authorization for Increasing Rates—Intent of Parties.* In determining whether a particular clause in a gas purchase contract authorizes increased rates, courts should endeavor to ascertain and give effect to the intent of the parties to the contract.

2. CONSTITUTIONAL LAW—*Contract Clause—Prohibition of State Impairment of Contract Obligations.* Under the contract clause of the U.S. Constitution (Art. I, § 10, cl. 1), prohibiting state impairment of contract obligations, legislation adjusting the rights and responsibilities of contracting parties must be upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption.

3. CONTRACTS—*Constitutional Contract Clause Challenges—Review of Legislation—Obligation of Courts.* In reviewing economic and social legislation against contract clause challenges, courts should defer to the legislature's judgment of the necessity and reasonableness of a particular measure.

4. OIL AND GAS—*Statutory Regulation of Rates—Constitutionality.* The Kansas Natural Gas Price Protection Act, K.S.A. 1980 Supp. 55-1401 *et seq.*, is a

reasonable and appropriate regulation of the natural gas industry; it is not unconstitutional under the contract clause of the United States Constitution, Article I, section 10, clause 1.

5. SAME—*Gas Purchase Contract—Indefinite Price Escalator Clause—Interpretation of Contract—Intent of Parties—Constitutionality of Statutory Regulations.* In a declaratory judgment action involving the construction of indefinite price escalator clauses in natural gas purchase contracts, the record is examined and it is *held*: 1) The parties intended that price increases under the contracts would be triggered by legislation such as the Natural Gas Policy Act of 1978, 15 U.S.C. § 3301 *et seq.*; 2) whether the price of natural gas increases under a certain contract is dependent upon the specific terms of that contract; 3) the contract provisions here involved were not effective to permit price escalation under § 105 of the Natural Gas Policy Act; 4) certain clauses in the contracts were "indefinite price escalator clauses" as defined by the Kansas Natural Gas Price Protection Act; and 5) the Kansas Natural Gas Price Protection Act is constitutional.

Appeal from Harper district court, division No. 2; CHAS. H. STEWART, judge. Opinion filed July 17, 1981. Affirmed.

Gary W. Davis, of Martin, Pringle, Fair, Davis & Oliver, of Wichita, argued the cause, and *Martin W. Bauer*, of the same firm, and *Clark Mandigo*, general counsel for Energy Reserves Group, Inc., were with him on the brief for the appellant.

Jerome T. Wolf, of Spencer, Fane, Britt & Browne, of Kansas City, Missouri, argued the cause, and *Basil W. Kelsey* and *Terry W. Schackmann*, of the same firm, *David S. Black*, general counsel, for the Kansas Power and Light Company, and *William C. Farmer*, of Smith, Shay,

Farmer & Wetta, of Wichita, were with him on the brief for the appellee.

Brian J. Moline, general counsel, and *Terence L. Mundorf*, assistant general counsel, were on the brief *amicus curiae* for the State Corporation Commission of the State of Kansas.

Robert L. Howard, of Foulston, Siefkin, Powers & Eberhardt of Wichita, was on the brief *amicus curiae* for Kansas Independent Oil and Gas Association.

The opinion of the court was delivered by

MILLER, J.: This is a declaratory judgment action involving the construction of the terms of two natural gas purchase contracts in the light of certain federal and state statutes.

The plaintiff, Energy Reserves Group (ERG), brought suit against the defendant, Kansas Power & Light Company (KPL), seeking judgment that ERG had the right to terminate the contracts. KPL, by counterclaim, sought judgment that it had committed no breach, and that ERG had no right to terminate the contracts. Upon an extensive documentary record, both parties moved for summary judgment. The trial court denied ERG's motion and granted that of KPL; ERG appeals.

The two gas purchase contracts in issue were executed on September 27, 1975, by Clinton Oil Company, predecessor of ERG, and KPL. One was a contract for the sale of gas produced directly from the wells; the other was a residue gas purchase contract for the sale of remaining gas after certain recovery and processing steps were completed. Under the contracts, KPL agreed to purchase natural gas for the life of the Spivey-Grabbs field, located in Harper and Kingman counties, or for the life of the processing plants associated with the field. All the gas involved was produced and sold within the State of Kansas and thus was intrastate gas.

Each contract contains identical provisions relating to government price escalation, price redetermination, com-

mission approval, and intent. These contract provisions are as follows:

The Government Price Escalator Clause

"6.7 If any federal or Kansas regulatory or governmental authority having jurisdiction in the premises shall at any time hereafter fix a price per MCF applicable to any natural gas of any vintage produced in Kansas, higher than the contract price then in effect under this gas contract, the price to be paid for gas thereafter shall be increased to equal such regulated price. In that event, the increased price shall be effective as of the date of action of the governmental or regulatory authority establishing the regulated price, or its effective date, whichever is later, subject to the provisions of Section 8 hereof."

Price Redetermination

"7.1 SELLER shall have the option to cause the price being paid for its gas by BUYER to be redetermined every two years, beginning in 1977. The request for a price redetermination shall be given in writing by SELLER to BUYER not later than 120 days prior to the beginning of the Contract Year for which the price redetermination is requested. Should such request not be given within the required time, SELLER shall be deemed to have waived its option for that two-year period only. The effective date of any price established by price redetermination shall be the beginning of the Contract Year, subject however, to the provisions of Section 8 hereof.

"7.2 Within the same one hundred twenty (120) days following SELLER'S request for a price redetermination, the parties shall mutually redetermine the price by considering three (3) contracts under which the highest prices are actually being paid for flowing gas ninety (90) days prior to the date the redetermined price is to be effective. The contracts

to be considered shall, (a) have a primary term of one (1) or more years, (b) be for gas produced in Kansas, (c) be for gas purchased by an interstate or intrastate company selling or using an average daily volume of 5,000 MCF or more of gas for the twelve (12) months period ending ninety (90) days prior to the date the redetermined price is to be effective, (d) not be for the purchase of Spivey-Grabbs Field gas by BUYER under contracts dated in 1975, (e) not include more than one contract of any one purchaser in any one field, and (f) not be for a price then subject to regulatory suspense or refunds. In determining the 'highest prices' being paid, and as they may apply to a fair market price under this contract, BUYER and SELLER shall make valid adjustments in pricing considerations, including but not limited to the heating value of the gas, and costs of gathering, compression and processing rights."

Commission Approval

"8.2 BUYER shall make application to the Kansas Corporation Commission for approval of the pass-on of any of such increased costs of gas not later than sixty (60) days prior to the date the applicable increase is scheduled to become effective, or within five days after the increase has been established by arbitration or by action of governmental or regulatory authorities. The failure of the Kansas Corporation Commission to approve a pass-on within sixty days after application by BUYER shall be deemed a rejection of the price increase for the purposes of this gas contract.

"8.3 BUYER shall have the option, to be exercised by written notice to SELLER not later than fifteen (15) days after the Kansas Corporation Commission shall have rejected any such pass-on, to pay the increased price and in such event the provi-

sions of this gas contract shall remain in effect. If BUYER does not elect to pay such increase then SELLER shall have the option to terminate this gas contract on thirty days prior written notice."

The Intent Clause

"23.1 It is the intention of the parties that the price adjustment provisions contained herein are solely for the purpose of compensating SELLER for the anticipated increase in its operating costs and for the anticipated increase in the value of its Natural Gas to be sold hereunder. It is understood that no price escalation, price redetermination or other pricing provision of this gas contract is for the purpose of offsetting any potential increase in SELLER'S Federal income tax liability as a result of the repeal of percentage depletion."

ERG invoked the price redetermination clause in 1977, and on November 27, 1977, the parties mutually accepted a price of $1.77 per MCF. This redetermined price was approved by the Kansas Corporation Commission and was the price paid by KPL during the calendar year 1978.

On November 9, 1978, Congress passed the Natural Gas Policy Act (NGPA), 15 U.S.C. §§ 3301-3432. This act (1) terminates the authority of the Federal Energy Regulatory Commission (FERC), successor to the Federal Power Commission, to prescribe rates for natural gas, and (2) establishes short term ceiling prices for various categories of natural gas. The sections of the act with which we are most concerned are as follows:

§ 2 (15 U.S.C. § 3301) is the definitions section. It defines "new well" as any well drilled after February 19, 1977, or the depth of which was increased by drilling after that date. It also defines "first sale" as any sale of natural gas "to any person for use by such person."

§ 102 (15 U.S.C. 3312) fixes the maximum lawful price for new natural gas. (The Section 102 price for new natural gas for the month of December 1978 was $2.078 per million BTU's).

§ 105 (15 U.S.C. 3315) fixes the ceiling price for gas sales under existing intrastate contracts. Subsection (b) (1) reads as follows:

"(b) Maximum lawful price

"(1) General rule

"Subject to paragraphs (2) and (3), the maximum lawful price under this section shall be the lower of—

"(A) the price under the terms of the existing contract, to which such natural gas was subject on November 9, 1978, as such contract was in effect on such date; or

"(B) the maximum lawful price, per million Btu's computed for such month under Section 3312 of this title (relating to new natural gas)."

§ 601 (15 U.S.C. § 3431) terminates the authority of the FERC to prescribe rates for both intrastate and interstate natural gas, beginning December 1, 1978. (The rates previously fixed by the Commission are left operative until that date.)

§ 602 (15 U.S.C. § 3432) provides that nothing in the NGPA "shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed" the maximum ceiling price fixed by the act.

On November 20, 1978, ERG notified KPL by letter that the gas price would increase on December 1, 1978, to the Section 102 price.

On December 1, 1978, the FERC announced interim regulations, one of which, effective on that date, provided that "[T]he establishment of maximum lawful prices under the NGPA shall not trigger indefinite price escalator clauses in existing intrastate or interstate contracts." 43 Fed. Reg. 56448, 56550 § 270.205(a) (Interim Regulations 1978).

KPL petitioned the KCC on December 7, 1978, for pass-through approval of the Section 102 rates demanded by ERG. KPL filed a supplemental petition relating to the pass-through of these increased prices on February 2, 1979. Seventy-five days from KPL's December 7th application was February 20, 1979.

On February 13, 1979, the FERC issued a notice of proposed changes in its rules; the interim regulations were continued in full force and effect during the comment period. 44 Fed. Reg. 16896 (March 20, 1979). The FERC, on March 13, 1979, issued Order No. 23, which withdrew the prohibition of the operation of indefinite price escalator clauses, retroactive to December 1, 1978. The Order reserves to state law the determination of whether such clauses operate in intrastate contracts. 44 Fed. Reg. 16895, 16904 (March 20, 1979).

Next in the series of events was the enactment by the Kansas legislature of the Kansas Natural Gas Price Protection Act, K.S.A. 1980 Supp. 55-1401 *et seq.* (which we shall refer to as the Kansas Act or the Price Protection Act), which became effective upon its publication in the official state paper on May 29, 1979. Some of the salient features of this act are as follows:

> 55-1402 defines "gas purchase contract" as "any contract under which natural gas is sold within the state of Kansas . . . (2) to any person for use by such person . . ." and it defines "indefinite price escalator clause" as "any provision of a gas purchase contract which provides for the establishment

or adjustment of the price of natural gas delivered under such contract by reference to other prices for natural gas. . . ."

55-1403 provides that the act shall apply only to contracts entered into before April 20, 1977.

55-1404 restricts the operation of indefinite price escalator clauses. With certain exceptions, it provides that:

> "[O]n or after December 1, 1978, the price allowed to be paid pursuant to federal legislation or any regulation by an agency implementing such legislation, or the price paid or to be paid for any sale of natural gas in the state of Kansas shall not be taken into account in applying any indefinite price escalator clause contained in any gas purchase contract subject to this act, to the extent that such contract provides for the sale in the state of Kansas, of gas produced within this state which was not committed or dedicated to interstate commerce on November 8, 1978. This section shall not require a reduction of any price contained in any gas purchase contract subject to this act below the price actually paid prior to the date of enactment of this act."

55-1408 provides that this act shall not limit the voluntary renegotiation of price provisions contained in natural gas purchase contracts.

55-1411 declares that the price limitations defined in this act shall terminate not later than December 31, 1984.

ERG, by letter dated June 5, 1979, notified KPL of its intent to terminate the contracts in thirty days, on July 5, 1979, based on (1) the failure of KPL to make application to the KCC for pass-on authority within five days of December 1, 1978, (2) the failure of KPL

to obtain KCC approval for the payment of the Section 102 price, and (3) the failure of KPL to pay the increased price. ERG contended that the pricing provisions of the NGPA triggered the government price escalation clause, § 6.7 of the contract, and that ERG was therefore entitled to the Section 102 price. KPL responded on June 13, 1979, denying that the government price escalator clause was triggered by the NGPA, claiming that 55-1404 of the Price Protection Act prevents the operation of the escalator clause, and further contending that KPL had not violated the contract and ERG had no right to terminate the contracts.

ERG filed its petition in the district court of Harper County on July 2, 1979, seeking a declaratory judgment that it had the right to terminate the contracts on the grounds set forth in its June 5 letter.

Next, on July 24, 1979, ERG wrote letters to KPL requesting that the price being paid under both contracts be redetermined under the price redetermination clauses of the contracts (§ 7, quoted above). KPL responded on July 27, stating in effect that K.S.A. 1980 Supp. 55-1404, a part of the Price Protection Act, prevents the operation of the price redetermination clauses in the contracts; therefore KPL could not agree to the requested price redetermination.

ERG then filed an amended petition in the trial court, including the claim that it was entitled to terminate the contracts because of KPL's refusal to renegotiate the price pursuant to the price redetermination clauses in the contracts. KPL answered, and also filed a counterclaim in which it sought a declaratory judgment that it had not breached the contract, that the contracts were still in effect, and that ERG had no lawful right to termination. Both parties attached to their pleadings copies of the contracts and of correspondence exchanged between them; both moved for summary judgment. Additional documents and affidavits were supplied the court in con-

nection with those motions, and the parties agreed that the facts were not in dispute.

After extensive oral argument and the submission of briefs, the trial court issued a lengthy and detailed memorandum opinion on April 11, 1980, ruling in substance: (1) that the governmental price regulation clauses in the contracts were intended to apply to rates fixed by a regulatory authority, and that such rates are distinguishable from ceiling prices established by the NGPA; (2) that the NGPA did not trigger the indefinite price escalator clauses in the contracts; (3) that the parties may voluntarily renegotiate prices, but that ERG cannot have an automatic increase under either the government price escalator clause or the price redetermination clause for the reason that such price escalation is prohibited by the Kansas Price Protection Act; (4) that the case cannot be decided without determining the constitutionality of the Kansas act; and (5) that the Kansas act does not violate the contract clause of the United States Constitution. The court denied ERG's motion for summary judgment, and sustained that of KPL. ERG appeals.

The first point raised is that the trial court erred in finding that the government price escalation clauses in the contracts were not intended to be triggered by enactments such as the NGPA. ERG's principal contention on this issue is that the trial court utilized far too narrow an analysis of the government price redetermination clauses; ERG claims that if the court had examined the intent of the parties, it would have concluded that the NGPA was the kind of enactment which was within the contemplation of the parties when they entered into the contracts.

The terms of the government price redetermination clause in the contracts before us are much broader than the clause found in the contracts in the case of *Mesa Petroleum Co. v. Kansas Power & Light Co.*, 229 Kan.

631, 629 P.2d 190 (1981). The escalator clause here refers to "any federal or Kansas regulatory, *or governmental authority.*" In *Mesa*, under the more limited escalator clause there contained, we found: "It is reasonable to assume that parties intended if Congress increased the maximum prices for which gas might be sold that this would fulfill the reference in [the government price escalator clause present in the Mesa contract] to action by any successor governmental authority." The intention of the parties is clearly expressed in the ERG-KPL contracts, which contain an "intent clause" not found in the Mesa-KPL contracts; that clause clearly states that the purpose and intention of the parties is to increase the price of gas for the purpose of compensating ERG not only for anticipated increases in operating costs, but also for anticipated increases in the value of its natural gas.

The reasoning of the Federal Energy Regulatory Commission in its March 4, 1980, opinion in *Independent Oil and Gas Association of West Virginia*, Opinion No. 77, Util. L. Rep. (CCH) ¶ 12,274, is useful here. The Commission reaffirmed its holding in Order No. 23, referred to above, which withdrew the prohibition of the operation of indefinite price escalator clauses, sometimes also referred to as area rate clauses. The Commission said:

> "The fundamental concept underlying Order 23 is that, in determining whether a particular clause authorizes collection of NGPA rates, the Commission will endeavor to ascertain and give effect to the intent of the parties to the contract. . . . [I]ntent is the controlling factor with respect to this issue. . . .
>
> "Our conclusion that the Commission is not limited to the 'four corners' of a contract in determining intent was arrived at after thorough consideration of the record developed in the rulemaking proceedings culminating in that order. . . . In view of the record developed in the rulemaking proceedings and

in light of the accumulated experience of the Commission in dealing with area rate clauses in a variety of settings, there is ample reason to believe that the intent of the parties to permit prices to escalate to the highest rates allowed by law—including statutory rates—may not, in many cases, have been fully reflected in the terms they chose. Since the words they used were a product of the then prevailing regulatory scheme under the Natural Gas Act, we must attempt to ascertain, to the extent possible, what the parties intended to accomplish in the context of that regulatory environment and to give effect to that intent in light of the changed circumstances brought about by enactment of the NGPA. . . .

"[W]e do not believe their intent should be thwarted merely because they failed to foresee that the Congress would assume the ratemaking function previously delegated to the Commission . . . ." pp. 14, 444-45.

As applied to the facts before us, the fundamental holding of Opinion 77 is that the Commission will not conclude that the transfer of the ratemaking function from the Commission to Congress—most likely unforeseen by the parties at the time the contract was drafted—operates to defeat the intent of the parties simply because they expressed that intent in the terms of the then prevalent ratemaking system. For similar reasoning applied under the old ratemaking procedures, see *Amoco Production Co. v. Kansas Power & Light Co.*, 505 F. Supp. 628 (D. Kan. 1980).

The ERG-KPL contracts were executed in 1975, when rates were prescribed by the Commission. The contracts, however, refer not only to regulatory bodies but to any "governmental authority having jurisdiction," and certainly the Congress is such a body. Viewing the instruments from their four corners, we conclude that the in-

struments are not ambiguous, and that the parties *intended* that the government price escalation clauses be triggered by enactments such as the NGPA.

Whether the contract price escalated from its November 9 level to the Section 102 level, however, is dependent upon the escalation clause in the contracts. In *Pennzoil Co. v. Federal Energy Regulatory Comm'n*, 645 F.2d 360 (5th Cir. 1981), discussing Section 105 of the NGPA, the court says:

> "If . . . the price on November 9th was less than section 102, under section 105(b)(1) the maximum lawful price is the current price provided for under the terms of the contract as long as it does not exceed the section 102 price. . . . [In such a] case, the intrastate contract price may escalate from its November 9th level to the section 102 level, *provided that the contract has a sufficient escalation mechanism.*" (Emphasis supplied.) pp. 374-75.

The final sentence of Section 6.7 of the ERG-KPL contracts provides that "[i]n that event [that a governmental authority fixes a higher price] the increased price shall be effective as of the date of action of the governmental or regulatory authority establishing the regulated price [November 9, 1978], or its effective date [December 1, 1978], *whichever is later. . . .*" (Emphasis supplied.) The November 9th price, then, continued until December 1, 1978, under the clear terms of the contracts.

Section 105(b)(1) of the NGPA fixes the maximum lawful price of intrastate gas as the lower of the Section 102 price or "the price under the terms of the existing contract, to which such natural gas was subject on November 9, 1978, as such contract was in effect on such date . . ." We hold that under the terms of the government price escalator clause in these contracts, and under the applicable section of the NGPA, the November 9th gas price (which was lower than the Section 102 price) did

not escalate. The rationale expressed in the *Mesa Petroleum Co.* case is fully applicable here. The NGPA did not trigger a price increase because the contracts herein did not contain a sufficient escalation mechanism.

Appellant also contends that the district court erred in granting summary judgment as there were genuine issues of material fact, necessitating an evidentiary hearing. The fact issues, however, relate entirely to the intent of the parties, and since we have resolved that issue from the wording of the contracts themselves, no fact issue remains for determination.

The resolution of these issues, however, does not determine this lawsuit. We must also consider the price redetermination provision of the contracts, ERG's attempt to utilize those clauses, and the effect of the Price Protection Act thereon. The price redetermination clause provides in substance that upon request of the seller, the parties shall mutually redetermine the price by considering three contracts under which the highest prices are actually being paid for flowing gas. The "weighted average price" being paid under the contracts shall then become the redetermined price.

K.S.A. 1980 Supp. 55-1402(*c*) provides:

> " 'Indefinite price escalator clause' means any provision of a gas purchase contract which provides for the establishment or adjustment of the price of natural gas delivered under such contract by reference to other prices for natural gas, for crude oil, or for refined petroleum products."

K.S.A. 1980 Supp. 55-1404 provides in substance that the price paid or to be paid for natural gas in the State of Kansas shall not be taken into account in applying any indefinite price escalator clause contained in any gas purchase contract subject to this act. The act applies to natural gas purchase contracts entered into before April 20,

1977, providing for the sale of natural gas produced in this state and not committed to interstate commerce.

ERG contends that the Kansas act does not apply because, in addition to the prices paid for natural gas under other contracts, the price redetermination clause here requires the parties to make adjustments with reference to other factors, including, but not limited to, the heating value of the gas, and costs of gathering, compression and processing rights. The primary thrust, however, of the price redetermination clause is to adjust and fix the price of the gas under these contracts based upon the price paid for natural gas under other contracts. The price redetermination clause in these contracts appears to fit precisely within the definition of "indefinite price escalator clause" included in the statute and set forth above. ERG's argument is not persuasive, and we hold that the Kansas act prohibits now, and at the time requested prohibited, price redetermination under the applicable section of the contracts. This issue cannot, as ERG suggests, be determined in a manner which would avoid the constitutional issue.

ERG contends that the Price Protection Act violates the contract clause set forth in Article 1, Section 10, of the Constitution of the United States. The contract clause reads as follows:

> "No State shall . . . pass any . . . Law impairing the Obligation of Contracts . . . ."

A memorandum opinion of the trial judge reflects his research and careful thought in this area. He says:

> "The constitutional bar against legislation 'impairing the obligation of contracts' has not been given literal, unconditional application, making it destructive of the public interest by depriving the states of appropriate powers such as the right to impose price controls. *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234 [,57 L.Ed.2d 727, 98 S.Ct. 2716] (1978).

"The constitutionality of state legislation that alters contractual obligations of private parties is solely dependent upon whether or not such legislation is based upon reasonable conditions and is of character appropriate to the public purpose justifying its adoption. Legislation that is both reasonable and necessary to serve a public purpose does not offend the contract clause. To this end, the Supreme Court has employed a balancing approach to resolve contract clause challenges. The Court has flexibly relied on several factors to determine the reasonableness of the legislative action. These include the severity of the legislation's impact on a private contract right, the scope and applicability of the legislation, and the importance of the public purpose that justifies its adoption.

"Here it is interesting to consider what the Court said in *United States Trust Co. v. New Jersey*, 431 U.S. 1 [, 52 L.Ed.2d 92, 97 S.Ct. 1505] (1977). I quote headnote 13 [52 L.Ed.2d at 95]:

> "'13. Although the states must possess broad power to adopt general regulatory measures without being concerned that private contracts will be impaired or even destroyed as a result, private contracts are not subject to unlimited modification under the states' police power for purposes of the contract clause of the U.S. Constitution (Art. I § 10, cl. 1), prohibiting state impairment of contract obligations; legislation adjusting the rights and responsibilities of contracting parties must be upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption, *but, as is customary in reviewing economic and social regulation, courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure.*' [Emphasis added.]

"KPL contends that the reasonableness of the Price Protection Act is quite clear in light of its important public purpose and the minimal contractual interest that it impairs. I agree, and here it is appropriate to look at what the Legislative Report which accompanied H.B. 2680 states:

> " 'Due to the changes in the Gas Pricing System brought about by NGPA, H.B. 2680 would have the effect of restricting somewhat abrupt and unanticipated increases in the price of old gas dedicated to intrastate commerce under certain gas purchase contracts which contain indefinite price escalator clauses.
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> " 'The NGPA of 1978 marked a radical reversal of the federal policy toward the pricing of natural gas. This law is directed toward increasing the price of gas, with the ultimate goal of deregulation of gas pricing. For many years the federal policy was directed toward pricing gas on a cost of service basis in interstate commerce. The new policy is to establish ceiling prices which will rise monthly to the point of final deregulation of many categories of natural gas production on December 31, 1984.
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will benefit beyond any expectations that they might have had only a few years ago and the consumers, already buffeted by rapidly increasing inflation, including spiraling utility costs, will pay. Natural gas prices will continue to increase in the foreseeable future.

" 'The Congress recognized this scenario and, as a result, specifically reserved to the states an area of price control applicable to intrastate gas sales, according to proponents.

" 'The proponents contended that H.B. 2680 represents an effort by the State of Kansas to minimize the impact on consumers of natural gas price increases of some intrastate gas from the present time through 1984. For a period of nearly six years, this bill would provide a modicum of restraint on some utility price increases.

" 'As a result of its hearings and deliberations, the majority of the Committee is strongly convinced that the single issue of the benefits to be derived by the affected Kansas consumers of natural gas clearly outweighs any adverse effects the gas producers or royalty owners said the bill might have. *Except where long-term, fixed price contracts are involved, the producers and royalty owners are benefiting significantly under the new NGPA. The bill merely prevents the producers from receiving the full amount of unanticipated gains that would be experienced.* Special Comm. on Energy and Natural Resources, *Report on H.B. 2680*, Exhibit A to Suggestions in Support of KPL's Cross Motion for Summary Judgment (Emphasis supplied).'

"The legitimate public purpose of the Price Protection Act cannot be questioned. See *Home Bldg. & L. Assn. v. Blaisdell*, 290 U.S. 398 at 444-45 [, 78 L.Ed. 413, 54 S.Ct. 231 (1934)]. In a time already facing

serious problems of inflation, Kansas has a bona fide interest in addressing, and hopefully controlling, the serious economic dislocations that a sudden introduction of significantly higher energy costs would produce. The federal government acknowledged the legitimacy of this public purpose by expressly reserving to the states the option to so act.

"Under the standards of *Allied Structural Steel*, and prior case law, the Price Protection Act is a reasonable path chosen to achieve this important public purpose. The relief is appropriately tailored to meet the conditions it addresses, and is neither overbroad nor overly harsh. See *Allied Structural Steel*, 438 U.S. at 244. It affects only old gas and gas for which a higher price has not yet been paid. The Price Protection Act merely prevents an automatic triggering of indefinite price escalator clauses.

"Additionally, the Price Protection Act is limited in time as well as scope. Its controls extend over a period of a few years to lessen the economic shock to citizens, businesses and institutions of this state, who are otherwise suddenly subject to significantly higher prices for natural gas that affects virtually every aspect of their lives. The measure chosen by Kansas does not seek forever to foreclose the introduction of those higher prices into the economy, nor to deny gas producers the ultimate increases in the purchase price of their resource. The legislation gradually spreads out over the NGPA's time period for gradual price deregulation, the ultimate, and perhaps inevitable, impact of those higher prices.

"The ramifications of the sudden introduction of these higher prices are clear. The Price Protection Act merely regulates these evils by graduating the introduction of higher natural gas prices into the Kansas economy. Some price increases are presently allowed, especially those that encourage new explora-

tion and production from higher cost or low yield sources. Negotiations for new contractual price provisions are permitted to guarantee a measure of fairness. Automatic price escalations, however, triggered by indefinite escalator clauses and unrelated to cost of production or factors of supply and demand, are postponed. A more reasonable and specifially tailored approach to the problem could hardly be imagined.

"In reviewing economic and social legislation against Contract Clause challenges, courts should defer to the legislature's judgment of the necessity and reasonableness of a particular meaure. *United States Trust Co. v. New Jersey*, 431 U.S. at 23; *East New York Bank v. Hahn*, 326 U.S. 320, [90 L.Ed. 34, 66 S.Ct. 69] (1945). Even without that presumption of reasonableness and necessity, the price Protection Act manifestly represents 'legislation adjusting the rights and responsibilities of contracting parties . . . upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption.' *Allied Structural Steel*, 438 U.S. at 244, quoting *United States Trust Co.*, 431 U.S. at 22; *Home Bldg. & L. Assn.*, 290 U.S. at 445-47.

"Both the nature of the regulation provided by H.B. 2680, and the commodity regulated, are high on the list of priorities of governmental restrictions and regulations. I refer to price regulation and energy. There is an abundance of precedent for price control legislation much more stringent than H.B. 2680, beginning with *Munn v. Illinois*, 94 U.S. 113 [, 24 L.Ed. 77] (1876), and continuing through the *Permian Basin Area Rate Cases*, 390 U.S. 747 [, 20 L.Ed.2d 312, 88 S.Ct. 1344] (1968), upholding an absolute prohibition on the operation of indefinite price escalator clauses. There is a very close connection with the manner the courts handle the contract clause of the U.S. Constitution and with the way

> they treat the due process clause of the Fourteenth Amendment. The Supreme Court has expressly stated that the states' power reasonably to regulate natural gas prices cannot seriously be questioned under the due process clause. As to the commodity being regulated, we would all have to be blind, deaf and dumb not to be aware that long before H.B. 2680 was enacted there was a national campaign to control all types of energy, including natural gas, which campaign or movement is still very much alive and can almost be classified as a crusade."

We agree with the district judge, and adopt the quoted portion of his memorandum opinion.

The NGPA constituted an entirely new and drastically different approach to the pricing of natural gas; it broke with the past, and substituted deregulation for close agency regulation under which the industry had operated for many years. Contract prices for natural gas on November 9, 1978, as disclosed by the several recent cases before us, varied from less than thirty cents per Mcf to more than $1.90 per Mcf. The Section 102 price for new gas and for natural gas produced on the outer continental shelf exceeded $2.00 per Mcf. The anticipated sudden escalation of intrastate gas prices threatened both gas and electric utility rates. The legislature was cognizant of this emergency situation when it considered and enacted the Kansas Natural Gas Price Protection Act. That act protects the public generally from an immediate increase in rates; with allowed monthly increases, the rate increase will be phased in over a period several years.

The legislation addresses an important public purpose. Under all of the attendant circumstances, we conclude that the legislation, and the tempering of price increases which it provides, are reasonable and appropriate.

ERG contends that the Kansas Act is retroactive to December 1, 1978, and, since it impairs the contract and disturbs the vested rights of ERG under the contract as of that date, it must fall. The statute obviously was intended to and does impair the rights of ERG under the contracts to invoke the price redetermination clause, and thus secure higher prices for its gas based upon prices paid for other gas. The date chosen for the retroactivity, December 1, 1978, is the date upon which the orders of FERC, regulating rates, ceased to be operative, and the provisions of the NGPA took effect.

The trial court concluded that the statute had no retroactive application. Since ERG did not attempt to invoke the price redetermination clause provisions of the contract until after the effective date of the statute, the application would appear to be primarily prospective only. However, ERG contends that it had the right under the contract to price redetermination, which rights vested upon the date the contract was executed, and that these rights were taken away when the Price Protection Act became effective, retroactive to December 1, 1978. The statute, as we have pointed out, was enacted under the police power of the state to regulate the intrastate price of natural gas. If the legislature could not make the statute retroactive to December 1, 1978, then it would have no effective way to control intrastate natural gas prices. Automatic escalator clauses, activated during that period, would nullify the powers of the state to protect its citizens in this important area. We conclude that the Kansas Act is an appropriate exercise of the police power of the state, that it was reasonable and fully justified under the circumstances, and that it is not unconstitutional upon the basis of its retroactivity.

Finally, ERG contends that the district court erred in failing to consider ERG's optional right to terminate the contracts. Its right to terminate depended upon (1) whether the price increased, and (2) whether KPL vio-

lated the contract terms. Since, as we have held, the price did not escalate, KPL did not violate the contract terms and ERG had no right to terminate the contracts.

We have carefully considered the arguments and the authorities cited by counsel, but we find them unpersuasive and we will not prolong this opinion by a recital thereof.

The judgment is affirmed.

APPENDIX B

IN THE DISTRICT COURT
OF HARPER COUNTY, KANSAS

No. 79 C 37

ENERGY RESERVES GROUP, INC.,
Plaintiff,

—VS—

THE KANSAS POWER AND LIGHT COMPANY,
Defendant.

MEMORANDUM OPINION

This is a breach of contract action wherein plaintiff Energy Reserves Group, Inc. (hereafter ERG) seeks a declaratory judgment that Kansas Power & Light Company (hereafter KPL) has breached two gas supply contracts between these parties. ERG seeks a judgment declaring the lawful termination of the contracts under the provisions thereof effective 30 days after each of two separate notices of breach and termination given by ERG. KPL has answered and counterclaimed for a declaratory judgment that it has not breached the contract, that the contractual terms still bind the parties, and that ERG has not lawfully terminated the contracts.

This matter is now before the Court on ERG's Motion For Summary Judgment pursuant to K.S.A. Sec. 60-256, and on defendant KPL's Cross Motion for Summary Judgment or [sic] its Counterclaim and for Declaratory Relief on plaintiff's claim against it.

STATEMENT OF UNCONTROVERTED FACTS

1. The Gas Purchase Contract (Exhibit A) and the Residue Gas Purchase Contract (Exhibit F) were executed as of September 17, 1975.

2. KPL and ERG mutually accepted a price redetermination under the contract on November 17, 1977.

3. KPL received the letters from ERG, dated June 5, 1979, which said letters are Exhibits D and H to the Amended Petition.

4. KPL sent letters dated June 13, 1979, which demonstrates that ERG and KPL are in disagreement as to the interpretation of the government provision clause of the contracts. Exhibits E and I to the Amended Petition.

5. KPL received letters from ERG dated July 25, 1979, August 2, 1979, August 2, 1979, and August 6, 1979, attached as Exhibits J, K, L and N respectively to the Amended Petition.

6. KPL sent a letter dated July 27, 1979 relating to the ERG requests for price redetermination. Exhibit M to the Amended Petition.

7. The NGPA was enacted and thereafter became effective on December 1, 1978.

8. KPL filed an application relating to a pass through of increased prices on December 7, 1978, and filed a supplemental application relating to the pass through of increased prices on February 2, 1979. By Order of November 9, 1979, the Kansas Corporation Commission stated that a pass through of increased prices as they relate to these applications were not approved.

9. The delivery and purchase of natural gas under the subject contracts involves intrastate sales of natural gas.

10. On November 20, 1978, ERG mailed a letter to KPL attached to the memorandum filed on February 7, 1980, which letter was received by KPL as evidenced by the signature of one of its agents.

ERG filed this action for a determination of whether defendant KPL was obligated to pay higher prices under the two price escalator clauses in the gas supply contracts between these parties. KPL has moved for summary judgment based upon Kansas legislation which it claims expressly forbids the type of price increases and redeterminations that ERG seeks. This legislation is the Natural Gas Price Protection Act. House Bill No. 2680, 1979 Kan. Session Laws 841, et seq. (Price Protection Act) In its Motion For Summary Judgment, ERG challenges the constitutionality of this particular legislation.

In the main, ERG bases its claim for higher prices on certain provisions of the Federal Natural Gas Policy Act of 1978 (NGPA), 15 USC, Secs. 3301, et seq. (Supp. 1979), which establishes new ceiling prices for natural gas, claiming that such provisions triggered the indefinite price escalator clauses in these parties' contracts. These clauses provide for an increased contract price if a governmental authority with jurisdiction "fixes" a price higher than the contract price then in effect.

Counsel for both sides of this controversy have thoroughly briefed and argued, pro and con, as to whether the terms of NGPA establishing new ceiling prices for natural gas triggered the indefinite price escalator clauses in these parties' contracts. Frankly, I am unable to see why the answer to this question is so difficult. There is simply no way to equate the terms of the contracts found in paragraph 6.7 of the Gas Purchase Contract and paragraph 8.5 of the Residue Gas Purchase Contract, which refer to any federal or Kansas regulatory or governmental authority fixing a price, to the terms of NGPA which establishes new ceiling prices for natural gas. ERG contends that the terms "fix," "regulate" and "establish," at least in a general way, all have the same or similar meanings. I believe there is a difference, however, what really distinguishes

the terms found in NGPA from the contract terms is the fact that one establishes a *ceiling* price and the other just simply refers to a fixed price. There is simply no way I can be convinced that NGPA triggered the indefinite price escalator clauses in these parties' contracts.

The remaining issues in this matter mainly concern the effect of the Kansas Natural Gas Price Protection Act, House Bill No. 2680, 1979 Session Laws 841, et seq. The NGPA contained the following provision:

> "Nothing in this Act shall affect the authority of any state to establish or enforce any maximum lawful price for the first sale of natural gas produced in such state which does not exceed the applicable maximum lawful price, if any, under Title I of the Act."

In apparent reliance upon this authority, the Kansas Legislature enacted the Kansas Natural Gas Price Protection Act. H.B. No. 2680, Ch. 171, 1 *et. seq.* L. 1979. The pertinent provisions of the Price Protection Act provide as follows:

> "Sec. 3. Only natural gas purchase contracts entered into before April 20, 1977, providing for the sale, within this state, of natural gas produced in this state and not committed or dedicated to interstate commerce on November 8, 1978, shall be subject to the provisions of this act."
>
> "Sec. 4. Except to the extent provided in sections 5 and 6, on or after December 1, 1978, the price allowed to be paid pursuant to federal legislation or any regulation by an agency implementing such legislation, or the price paid or to be paid for any sale of natural gas in the State of Kansas shall not be taken into account in applying any indefinite price escalator clause contained in any gas purchase contract subject to this act, to the extent that such contract provides for the sale in the State of Kan-

sas, of gas produced within this state which was not committed or dedicated to interstate commerce on November 8, 1978. This section shall not require a reduction of any price contained in any gas purchase contract subject to this act below the price actually paid prior to the date of enactment of this act."

"Sec. 5. Notwithstanding the restriction on the operation of indefinite price escalator clauses imposed by section 4 of this act, after March 1, 1979, such indefinite price escalator clauses in gas purchase contracts subject to this act may be given effect in accordance with their terms to the extent that the price payable under such contracts is not increased above the maximum price such gas would receive if it qualified under section 109(b) of the Natural Gas Policy Act of 1978. The maximum price shall be calculated on a monthly basis. Nothing in this section shall be construed to apply to gas produced from new wells, new reservoirs or stripper wells as defined by this act or to gas produced from any well located at a depth of more than 15,000 feet."

"Sec. 6. Notwithstanding the restriction on operation of indefinite price escalator clauses in gas purchase contracts imposed by sections 4 and 5 of this act, after March 1, 1979, with respect to natural gas which is subject to this act, and which qualifies as gas produced from new wells, new reservoirs or stripper wells as defined in this act and gas which is produced from wells located at a depth of more than 15,000 feet, such indefinite price escalator clauses may be given effect in accordance with their terms to the extent that the price payable under such contracts is not increased above the maximum price such gas would receive if it had been committed or dedicated to interstate commerce. The maximum price shall be calculated on a monthly

basis. If the parties to the contract cannot agree as to the category of gas for which such gas qualifies under the terms of the Natural Gas Policy Act of 1978, then such category determination shall be made by the commission."

"Sec. 8. Nothing contained in this act shall prevent or limit the voluntary renegotiation of price provisions contained in natural gas purchase contracts."

"Sec. 11. All price limitations as defined in this act shall terminate not later than December 31, 1984. The commission shall monitor and report to the legislature at the commencement of each regular session in each year this act remains in operation, the effect of this act upon the availability of natural gas in this state . . .

"Sec. 15. If any sentence, clause, subsection, or section of this act is held unconstitutional or invalid by any court of competent jurisdiction it shall be conclusively presumed that the legislatiure would have enacted the remainder of the act not so held unconstitutional or invalid.

"Sec. 16. This act shall take effect and be in force from and after its publication in the official state paper."

KPL allges that by reason of the above-quoted provisions of the Price Protection Act (H.B. 2680), provisions for increased prices for the gas or the right of termination are unenforceable by ERG.

To counter the claims of KPL, ERG makes and argues contentions under five separate headings. For the sake of order and, I hope, clarity, I will take up these contentions in the same order they are argued in ERG's Memorandum in support of its Motion For Summary Judgment.

New Contract—Under Sec. 3 of H.B. 2680, only contracts entered into before April 20, 1977 are subject

to the limitations allegedly created by the act. ERG contends the parties formed a new contract effective November 27, 1977, when KPL offered and ERG accepted a new price to be paid for the gas produced by ERG. That the agreement of November 27, 1977 is a substitute contract which replaced the parties' prior agreement.

I am forced to agree with KPL that ERG's argument that the parties entered into new contracts in 1977, due to their acceptance of price redeterminations pursuant to the original contracts, can hardly be taken seriously. The letters of agreement accepting the price redeterminations pursuant to the original contracts state that KPL is performing under the terms of gas purchase contracts dated September 27, 1975, and that:

> "In accordance with paragraph 7.2 (9.2 for residue gas contract) these parties have agreed that the redetermined price to be paid for gas purchased under said contracts effective November 27, 1977 shall be . . ." See Exhibits B and G to ERG's Amended Petition.

The very language quoted above belies the claim that the redetermination of price had the effect of a new contract. So there will be no doubt about my decision of this particular contention, I find and hold that the redetermination of price was no more than a procedure provided by the original contracts to amend or modify the original contracts and in no manner constituted a new contract. Texas Gas Transmission Corp. vs. Shell Oil Co., 363 U.S. 263 (1960).

Stripper Wells—ERG endeavors to strengthen its contentions that KPL has breached the contracts in question and for this reason ERG is entitled to a judgment terminating the contracts, by making the point that a part of the gas provided under the contracts constitutes gas produced from stripper wells and for this reason the restrictive provisions of H.B. 2680 do not apply. At

this stage of the case there is no way on earth this court could intelligently rule on this contention, simply because there is no determination by any governmental agency as to what wells being produced by ERG under the contracts in question constitute stripper wells (NGPA Sec. 108(b) specifically provides that stripper well gas only includes that gas so designated by the Federal Energy Regulating Commission pursuant to 15 U.S.C. Sec. 3413 Supp. 1979), nor is there actually any claim by ERG enumerating or describing certain wells as stripper wells. ERG makes a vague claim that a substantial amount of the gas being delivered to KPL is stripper well gas and that KPL by reason of the processing and taking delivery of gas, has knowledge of what wells are producing as stripper wells. KPL flatly denies that it has such information. Under the situation as it now stands, at least as far as this court is concerned, I am unable to see how ERG's request for a price redetermination, even conceding such request was limited to stripper wells, could possibly set up a situation giving ERG the right to demand a termination of the contracts. ERG is simply not in a position to demand a redetermination of the price of gas being produced from stripper wells when there has been no determination whatsoever that gas is being produced from stripper wells. It seems to me that ERG's argument on stripper wells is spurious. I would think ERG must at least be able to say to KPL "We have X number of stripper wells. They are described and located as follows ———. We demand a redetermination of price as to the gas being produced from these wells and being delivered to you under the terms of the contracts." I am forced to agree with KPL that the matter of stripper wells is outside the pleadings and that the question of whether there are "stripper wells" from which KPL is purchasing gas is not now before the Court.

Other than for what I have said in the foregoing paragraph, I see no legal reason why ERG would not be

entitled to a price redetermination for gas produced from stripper wells. As an aside, I will add that I would think that before this matter can become an issue, the parties must agree on the facts as to stripper wells or engage in much discovery.

Price Redetermination Process—The gist of ERG's argument under this heading is that the provisions of H.B. 2680 do not excuse KPL from engaging in price redetermination. ERG's argument is at least a two-pronged approach. It first contends that by Section 4 of H.B. 2680, the Kansas Legislature merely sought to preclude parties from considering the NGPA fixed prices or prices involved in other sales of natural gas produced in Kansas and did not actually preclude price redetermination. I have been unable to arrive at any conclusion other than that the Legislature had in mind the exact type price redetermination clause as found in paragraph 7.2 and paragraph 9.2 in the contracts when it approved and passed H.B. 2680 and fully and intentionally intended to prevent the operation of indefinite price escalator clauses in gas purchase contracts covered by H.B. 2680. For ERG to argue that the wording of H.B. 2680 does not preclude the redetermination of price but only precludes the method, when we consider that the method we speak of is the only one provided for in the contracts, just doesn't jibe. The only way this court or any other court could hold that H.B. 2680 does not preclude price redetermination as provided for in paragraphs 7.2 and 9.2 of the contracts is to hold H.B. 2680 unconstitutional. We will take that question up later. I am fully aware that there is an exception clause contained in H.B. 2680. I refer to Sec. 5, however, as a practical matter, it is not involved in this controversy.

I fully agree with ERG when it maintains that price redetermination is consistent with Sec. 8 of H.B. 2680, which permits voluntary renegotiation of price provisions contained in the contracts. However, I must agree with

KPL when it says "ERG, however, does not seek a voluntary renegotiation of price, rather, it seeks to enforce the price provisions found in paragraphs 7.2 and 9.2 of the contracts." I fail to find any evidence in the record showing that ERG has ever requested KPL to voluntarily renegotiate the price provisions contained in the contracts, as provided by Sec. 8 of H.B. 2680. This failure of KPL to enter into an agreement to redetermine or renegotiate price provisions of the contracts do not constitute a breach or give ERG the right to terminate the contracts.

Termination—Here ERG argues the proposition that when faced with a constitutional challenge to a statute, the Court should ascertain whether a construction of the statute is fairly possible by which the constitutional question may be avoided. What I have said under the headings New Contract, Stripper Wells and Price Redetermination Process clearly demonstrates that I am unable to resolve this controversy in a manner that avoids the constitutional issue.

Constitutionality—ERG contends H.B. 2680 is unconstitutional as a violation of Art. 1, P 10 of the U.S. Constitution which prohibits the states from passing any law impairing the obligation of contracts. There seems to be a difference of opinion between the parties regarding whether or not H.B. 2680 had any retroactive application in connection with the rights of the parties under the provisions of the contracts. As I see the situation it had no retroactive application and it is my opinion that the cases that have been decided in the main on this point simply do not apply. At least, as far as we know the facts in this controversy, we are dealing with prospective legislation.

The constitutional bar against legislation "impairing the obligation of contracts" has not been given literal, unconditional application, making it destructive of the public interest by depriving the states of appropriate

powers such as the right to impose price controls. (Allied Structural Steel Co. vs. Spannus, 438 U.S. 234 (1978)).

The constitutionality of state legislation that alters contractual obligations of private parties is solely dependent upon whether or not such legislation is based upon reasonable conditions and is of character appropriate to the public purpose justifying its adoption. Legislation that is both reasonable and necessary to serve a public purpose does not offend the contract clause. To this end, the Supreme Court has employed a balancing approach to resolve contract clause challenges. The Court has flexibly relied on several factors to determine the reasonableness of the legislative action. These include the severity of the legislation's impact on a private contract right, the scope and applicability of the legislation, and the importance of the public purpose that justifies its adoption.

Here it is interesting to consider what the Court said in *United States Trust Co. vs. New Jersey*, 431 U.S. 1. I quote Headnote 13:

> "13. Although the states must possess broad power to adopt general regulatory measures without being concerned that private contracts will be impaired or even destroyed as a result, private contracts are not subject to unlimited modification under the states' police power for purposes of the contract clause of the U.S. Constitution (Art. 1, P 10) prohibiting state impairment of contract obligations; legislation adjusting the rights and responsibilities of contracting parties must be upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption, *but as is customary in reviewing economic and social regulation, courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure.*"

KPL contends that the reasonableness of the Price Protection Act is quite clear in light of its important public purpose and the minimal contractual interest that it impairs. I agree, and here it is appropriate to look at what the Legislative Report which accompanied H.B. 2680 states:

> "Due to the changes in the Gas Pricing System brought about by NGPA, H.B. 2680 would have the effect of restricting somewhat abrupt and unanticipated increases in the price of old gas dedicated to intrastate commerce under certain gas purchase contracts which contain indefinite price escalator clauses."
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> "Proponents believe that as a result of this legislation, many producers of natural gas, especially those whose contracts contain indefinite price escalator clauses, will reap unanticipated, windfall financial benefits. These benefits bear no real relationship to the costs of production of new gas, and are not even remotely related to old gas production costs. They accrue solely because of the reversal of federal policy."
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"The Congress recognized this scenario and, as a result, specifically reserved to the states an area of price control applicable to intrastate gas sales, according to proponents."

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"As a result of its hearings and deliberations, the majority of the Committee is strongly convinced that the single issue of the benefits to be derived by the affected Kansas consumers of natural gas clearly outweighs any adverse effects the gas producers or royalty owners said the bill might have . . . *Except where long-term, fixed price contracts are involved, the producers and royalty owners are benefiting significantly under the new NGPA. The bill merely prevents the producers from receiving the full amount of unanticipated gains that would be experienced.* Special Comm. on Energy and Natural Resources, *Report on H.B. 2680*, Exhibit A to Suggestions in support of KPL's Cross Motion for Summary Judgment (Emphasis supplied).

The legitimate public purpose of the Price Protection Act cannot be questioned. See *Home Building & Loan Assn. vs. Blaisdell*, 290 U.S. 398 at 444-45. In a time already facing serious problems of inflation, Kansas has a bona fide interest in addressing, and hopefully con-

trolling, the serious economic disiocations that a sudden introduction of significantly higher energy costs would produce. The federal government acknowledged the legitimacy of this public purpose by expressly reserving to the states the option to so act.

Under the standards of *Allied Steel* and prior case law, the Price Protection Act is a reasonable path chosen to achieve this important public purpose. The relief is appropriately tailored to meet the conditions it addresses, and is neither overbroad nor overly harsh. See *Allied Steel*, supra, 98 S. Ct. at 2722. It affects only old gas and gas for which a higher price has not yet been paid. The Price Protection Act merely prevents an automatic triggering of indefinite price escalator clauses.

Additionally, the Price Protection Act is limited in time as well as scope. Its controls extend over a period of a few years to lessen the economic shock to citizens, businesses and institutions of this state, who are otherwise suddenly subject to significantly higher prices for natural gas that affects virtually every aspect of their lives. The measure chosen by Kansas does not seek forever to foreclose the introduction of those higher prices into the economy, nor to deny gas producers the ultimate increases in the purchase price of their resource. The legislation gradually spreads out over the NGPA's time period for gradual price deregulation, the ultimate, and perhaps inevitable, impact of those higher prices.

The ramifications of the sudden introduction of these higher prices are clear. The Price Protection Act merely regulates these evils by graduating the introduction of higher natural gas prices into the Kansas economy. Some price increases are presently allowed, especially those that encourage new exploration and production from higher cost or low yield sources. Negotiations for new contractual price provisions are permitted to guarantee a measure of fairness. Automatic price escalations, how-

ever, triggered by indefinite escalator clauses and unrelated to cost of production or factors of supply and demand, are postponed. A more reasonable and specifically tailored approach to the problem could hardly be imagined.

In reviewing economic and social legislation against Contract Clause challenges, courts should defer to the legislature's judgment of the necessity and reasonableness of a particular measure. *United States Trust*, supra, 97 S. Ct. at 1518; *East New York Savings Bank vs. Hahn*, 326 U.S. 230 (1945). Even without that presumption of reasonableness and necessity, the Price Protection Act manifestly represents "legislation adjusting the rights and responsibilities of contracting parties . . . upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption." *Allied*, supra, 98 S. Ct. at 2722, quoting *United States Trust*, supra, at 1518; *Blaisdell*, supra, 290 U.S. at 445-47.

Both the nature of the regulation provided by H.B. 2680, and the commodity regulated, are high on the list of priorities of governmental restrictions and regulations. I refer to price regulation and energy. There is an abundance of precedent for price control legislation much more stringent than H.B. 2680, beginning with *Munn vs. Ill.*, 94 U.S. 113 (1876) and continuing through the *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), upholding an absolute prohibition on the operation of indefinite price escalator clauses. There is a very close connection with the manner the courts handle the contract clause of the U.S. Constitution and with the way they treat the due process clause of the Fourteenth Amendment. The Supreme Court has expressly stated that the states' power reasonably to regulate natural gas prices cannot seriously be questioned under the due process clause. As to the commodity being regulated, we would all have to be blind, deaf and dumb not to be aware that long before H.B. 2680 was enacted

there was a national campaign to control all types of energy, including natural gas, which campaign or movement is still very much alive and can almost be classified as a crusade.

Both parties in this case have been helpful to this court, having filed exhaustive briefs citing many cases to substantiate their contentions. I believe I have read all of them. I suppose I could go on for 15 more pages but I see no reason for doing so. This type of controversy is not new. I was extremely interested in a Supreme Court case decided in 1918. I speak of *Union Dry Goods Co. vs. Georgia Public Service Corp.*, 218 U.S. 372. While there may be technical and superficial differences between the controversy in Union Dry Goods Co. and that between ERG and KPL, basically the same principles are involved. I will not be so presumptuous in this matter to say what the Court did in Union Dry Goods Co. but at least it does at least apply in part. I quote:

> "Except for the seriousness with which this claim has been asserted and is now pursued into this court, the law with respect to it would be regarded as so settled as not to merit further discussion."

In accordance with what has been said above, this court finds and determines that the correct interpretation and construction of the contracts in question extend no right to plaintiff to terminate the contracts and that both contracts remain valid, extending to the parties the benefits and rights provided therein and, in turn, obligating the parties in connection with the duties and obligations contained therein. Further, that nothing contained in NGPA triggered a price increase for gas being delivered by ERG to KPL. The Court further finds and determines that the effect of H.B. 2680 on the contracts is to temporarily make the Price Redetermination Provisions of the contracts inoperative, with the exception that H.B. 2680 does permit the operation of indefinite price escalator clauses in these contracts for the

sale of old intrastate gas up to the NGPA Sec. 109 ceiling price. The Court further finds that H.B. 2680 as it applies to the contracts in question does not violate the contract clause of the United States Constitution, Art. 1, P 10, nor the due process provisions of the 14th Amendment. The Court further finds that nothing in the statutes mentioned or in the contracts prevent the parties from voluntarily renegotiating the price provisions contained in the contracts. In accordance with the above findings and holdings, the Motion of Plaintiff for Summary Judgment is overruled and the Motion of the Defendant for Summary and/or Declaratory Judgment is sustained.

Dated April 11, 1980.

/s/ Chas. H. Stewart
District Judge

APPENDIX C

IN THE DISTRICT COURT
OF HARPER COUNTY, KANSAS
NINETEENTH JUDICIAL DISTRICT

No. 79 C 37

ENERGY RESERVES GROUP, INC.,
Plaintiff,

—VS—

THE KANSAS POWER AND LIGHT COMPANY,
Defendant.

MEMORANDUM OPINION

This matter is before the Court on Plaintiff's Motion To Reconsider and to Alter and Amend Judgment. I will consider the matter in the same order it was presented.

Intent of the Parties—Government Regulation Clauses. There is no way I can consider any part of these contracts as ambiguous. It has not been denied that the contracts were prepared by ERG. It would have been a simple matter to have used the terms "fix a ceiling price" in the wording of paragraphs 6.7 and 8.5 if that is what was intended. Or if the intention of the parties was that ERG was to receive consideration in the form of the highest permissible price for the natural gas delivered under the contracts, then it would have been quite a simple matter to have made the contracts read to that effect.

I cannot agree that the Intent Clause of the contracts lends weight to ERG's contention that NGPA triggered an escalation of price. The Intent Clause of these contracts clearly relates to the Price Redetermination Clause in the contracts. I fully agree that the Intent Clause as it applies to the Price Redetermination Clause means and intends what it says in plain language and that is

that the price to be paid for the gas should be redetermined as provided for the purpose of compensating the seller for the anticipated increase in its operating costs and for the anticipated increase in the value of its natural gas to be sold hereunder. Here we abruptly run up against the actions of the Kansas Legislature and the constitutional question, which to my way of thinking is the one and only question of substance in this lawsuit.

Price Redetermination Provision. I have carefully read the Memorandum Briefs submitted by ERG in connection with the Motion now before the Court, also I have had the advantage of reviewing the oral argument presented by Mr. Davis. From these I went back and read my Memorandum Opinion. It is my conclusion that there is nothing to add to what I have already said.

Stripper Well Gas. I must adhere to what I said in my Memorandum Opinion regarding the attempt to inject an issue regarding stripper well gas. I agree thoroughly with what KPL says on page 6 of its Response of KPL to ERG's Memorandum in Support of ERG's Motion To Reconsider and To Alter and Amend Judgment. I quote: "ERG fails to disclose what volume of gas, if any, is stripper gas, and what total price it asks for that gas. ERG failed to do the obvious in this action if its claim were truly bona fide—simply charge KPL for the amount of gas it claimed was stripper gas so that KPL might perform under its contract as ERG suggests that it should." I have a suspicion that I could probably have disposed of the stripper well issue in a manner somewhat similar to Judge Duckworth's disposal of the new well issue in the Mesa vs. KPL case. As a matter of fact, I suppose I have disposed of it in a similar manner. The only difference is that it took me longer to say it.

The Constitutional Question. Without bragging or complaining, I wish to say I have spent the better part of several days reviewing the contention of ERG that

Kansas Natural Gas Price Protection Act, at least insofar as it purports to negate the Price Redetermination Clause in the contracts in question, is unconstitutional. My conclusion is that I have very plainly and to the best of my ability set down my reasons for holding the statute constitutional and I frankly see no good reason for saying more. I must adhere to what was said in my Memorandum Opinion.

The Motion of the Plaintiff Requesting this Court To Reconsider and To Alter and Amend Judgment is overruled. (This is not entirely true as I have reconsidered the matter.) Counsel for Defendant will please prepare an appropriate journal entry which I assume will cover the judgment as well as the ruling above. Judgment will be effective when the journal entry is filed.

Dated July 11, 1980.

/s/ Chas. H. Stewart
District Judge

APPENDIX D

IN THE DISTRICT COURT
OF HARPER COUNTY, KANSAS

No. 79 C 37

ENERGY RESERVES GROUP, INC.,
Plaintiff,

—VS—

THE KANSAS POWER AND LIGHT COMPANY,
Defendant.

JOURNAL ENTRY

There is a breach of contract action wherein plaintiff Energy Reserves Group, Inc. (hereafter ERG) seeks a declaratory judgment that The Kansas Power and Light Company (hereafter KPL) has breached two gas supply contracts between these parties. ERG seeks a judgment declaring the lawful termination of the contracts under the provisions thereof effective thirty (30) days after each of two separate notices of breach and termination given by ERG. KPL has answered and counterclaimed for a declaratory judgment that it has not breached the contracts, that the contractual terms still bind the parties, and that ERG has not lawfully terminated the contracts.

Having examined the briefs and exhibits of the parties, and having heard oral argument of counsel, and being fully advised in the premises, the Court makes the following findings of fact and conclusions of law:

FINDINGS OF FACT

1. The Gas Purchase Contract (Exhibit A) and the Residue Gas Purchase Contract (Exhibit F) were executed as of September 17, 1975.

2. KPL and ERG mutually accepted a price redetermination under the contract on November 17, 1977.

3. KPL received the letters from ERG, dated June 5, 1979, which said letters are Exhibits D and H to the Amended Petition.

4. KPL sent letters dated June 13, 1979, which demonstrate that ERG and KPL are in disagreement as to the interpretation of the government provision clause of the contracts. Exhibits E and I to the Amended Petition.

5. KPL received letters from ERG dated July 25, 1979, August 2, 1979, August 2, 1979, and August 6, 1979, attached as Exhibits J, K, L and N respectively to the Amended Petition.

6. KPL sent a letter dated July 27, 1979 relating to the ERG requests for price redetermination. Exhibit M to the Amended Petition.

7. The NGPA was enacted and thereafter became effective on December 1, 1978.

8. KPL filed an application relating to a pass through of increased prices on December 7, 1978, and filed a supplemental application relating to the pass through of increased prices on February 2, 1979. By Order of November 9, 1979, the Kansas Corporation Commission stated that a pass through of increased prices as they relate to these applications were not approved.

9. The delivery and purchase of natural gas under the subject contracts involves intrastate sales of natural gas.

10. On November 20, 1978, ERG mailed a letter to KPL attached to the memorandum filed on February 7, 1980, which letter was received by KPL as evidenced by the signature of one of its agents.

11. ERG has failed to disclose what volume of gas, if any, is stripper gas, and what total price it asks for that gas, nor has ERG charged KPL for the amount of gas it claimed was stripper gas so that KPL might perform under its contracts as ERG suggests that it should.

CONCLUSIONS

1. The contracts before the Court are not ambiguous.

2. The Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. Sections 3301, et seq. (Supp. 1979), which establishes new ceiling prices for natural gas, does not trigger price escalations under paragraph 6.7 of the Gas Purchase Contract and paragraph 8.5 of the Residue Gas Purchase Contract, which provide for price escalations based upon any federal or Kansas regulatory or governmental authority fixing a price.

3. The parties before the Court did not enter into new contracts on November 27, 1977, when KPL offered and ERG accepted a new price to be paid for the gas produced by ERG for the reason that such redetermination of price was no more than a procedure provided by the original contracts to amend or modify the original contracts and in no manner constituted a new contract that H.B. 2680 does not regulate.

4. ERG's claim of breach based upon deliveries of stripper well gas is outside the pleadings and the question of whether there are "stripper wells" from which KPL is purchasing gas is not now before the Court for the reason that ERG has not perfected its claim based on these facts.

5. ERG may not demand a redetermination of the price of gas being produced from stripper wells when there has been no government determination whatsoever that gas is being produced from stripper wells.

6. The Kansas Legislature had in mind the exact type price redetermination clause as found in paragraph 7.2

and paragraph 9.2 in the contracts herein when it approved and passed H.B. 2680 and fully and intentionally intended to prevent the operation of indefinite price escalator clauses in gas purchase contracts covered by H.B. 2680.

7. H.B. 2680 temporarily makes the price redetermination provisions of the contracts inoperative, with the exception that H.B. 2680 does permit the operation of indefinite price escalator clauses in these contracts for the sale of old intrastate gas up to the NGPA Section 109 ceiling price.

8. Nothing in the contracts or in H.B. 2680 prevents the parties from voluntarily renegotiating the price provisions contained in the contracts.

9. KPL's failure to enter into an agreement to redetermine or renegotiate price provisions of the contracts does not constitute a breach or give ERG the right to terminate the contracts.

10. ERG has never requested KPL to voluntarily renegotiate the price provisions contained in the contracts, as provided by Section 8 of H.B. 2680.

11. The Court cannot interpret the contracts or H.B. 2680 in such a manner as to avoid the constitutional question surrounding H.B. 2680.

12. H.B. 2680 does not have retroactive application in connection with the rights of the parties under the provisions of the subject contracts.

13. The Price Protection Act is based upon reasonable conditions and is of a character appropriate to the legitimate public purpose that justifies its adoption.

14. As it applies to the contracts in question, H.B. 2680 does not violate the contract clause of the United States Constitution, Article I, Clause 10, nor the due process provisions of the Fourteenth Amendment.

15. The correct interpretation and construction of the contracts in question and the controlling law extend no right to plaintiff to terminate the contracts, and both contracts remain valid, extending to the parties the benefits and rights provided therein and, in turn, obligating the parties in connection with the duties and obligations contained therein.

16. The motion of plaintiff for summary judgment is overruled and the motion of defendant for summary judgment and/or declaratory judgment is sustained.

17. The motion of plaintiff requesting this Court to reconsider and to alter and amend judgment is overruled.

/s/ Charles H. Stewart
District Judge

STATE OF KANSAS)
) ss:
HARPER COUNTY)

I, Olive L. Ghormley, Clerk of the District Court of Harper County, do hereby certify the within document to be a full, true and correct copy of the original document as the same appears of record and now on file in said Court.

WITNESS MY HAND and official seal at Anthony, Kansas this 30 day of October 1980.

/s/ Olive L. Ghormley
OLIVE L. GHORMLEY
Clerk of the District Court

APPENDIX E

IN THE SUPREME COURT
OF THE STATE OF KANSAS

No. 80-52677-AS

ENERGY RESERVES GROUP, INC.,
Appellant

v.

KANSAS POWER & LIGHT CO.
Appellee

You are hereby notified of the following action taken in the above entitled case:

MOTION FOR REHEARING, RECONSIDERATION AND MODIFICATION.

THIS MOTION IS CONSIDERED AND DENIED.

Date September 23, 1981

Yours very truly,

LEWIS C. CARTER
Clerk, Supreme Court

APPENDIX F

IN THE SUPREME COURT OF THE STATE OF KANSAS

No. 80-52,677

ENERGY RESERVES GROUP, INC.,
Appellant,

vs.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Energy Reserves Group, Inc., the appellant above-named, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of the State of Kansas, affirming the granting of the Motion for Summary Judgment filed by the Kansas Power and Light Company and denying the Motion for Summary Judgment filed by Energy Reserves Group, Inc. The decision and judgment of the Supreme Court of the State of Kansas was entered on July 17, 1981 and thereafter a timely Motion for Rehearing was denied on September 23, 1981.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

Respectfully submitted,

WUNSCH, WUNSCH & GAUMER
120 Avenue B West
P. O. Box 473
Kingman, Kansas 67068

Clark Mandigo
General Counsel
ENERGY RESERVES GROUP, INC.

MARTIN, PRINGLE, FAIR, DAVIS
& OLIVER

By /s/ Martin W. Bauer
Gary W. Davis
MARTIN W. BAUER
300 Page Court
220 West Douglas
Wichita, Kansas 67202
(316) 265-9311
Attorneys for Plaintiff-
Appellant

CERTIFICATE OF SERVICE

and

NOTARIZED STATEMENT OF FILING

The undesigned, counsel of record for Appellant, Energy Reserves Group, Inc. and an attorney admitted to the bar of the Supreme Court of the United States, hereby avers and states that to the best of his knowledge an appropriate number of copies of the "Notice of Appeal to the Supreme Court of the United States" were deposited in the United States Mail at the Wichita, Kansas, United States Post Office on the 8th day of December, 1981, at approximately 12:30 p.m. with first class postage prepaid and properly addressed to the Clerk of the Supreme Court of Kansas, Clerk of the District Court, Harper County, Kansas and the counsel of record for each party separately represented, all within the time and in the manner permitted for such filings by Supreme Court Rules, addressed as follows:

Clerk of the Court
Supreme Court of Kansas
Kansas Judicial Center
Topeka, Kansas 66603

Clerk of the Court
Harper County
Anthony, Kansas 67003

Basil W. Kelsey
Jerome T. Wolf
Spencer, Fane, Britt & Brown
106 West 14th Street
Kansas City, Missouri 64105

William C. Farmer
Smith, Shay, Farmer & Wetta
830 Olive Garvey Building
Wichita, Kansas 67202

Larry Rapp
Foulston, Siefkin, Powers & Eberhardt
700 Fourth Financial Center
Wichita, Kansas 67202

Brian J. Moline
General Counsel
State Corporation Commission
4th Floor, State Office Building
Topeka, Kansas 66612.

/s/ Martin W. Bauer
MARTIN W. BAUER

STATE OF KANSAS)
) ss.
COUNTY OF SEDGWICK)

Subscribed and sworn to before me, in my presence, this 8th day of December, 1981, a Notary Public in and for the State of Kansas.

/s/ Raynell Ewing
Notary Public

My appointment expires: Dec. 28, 1985

APPENDIX G

SUPREME COURT OF THE UNITED STATES

No. A-513

ENERGY RESERVES GROUP, INC.,
Applicant
v.
KANSAS POWER AND LIGHT COMPANY

ORDER

UPON CONSIDERATION of the application of counsel for the applicant,

IT IS ORDERED that the time for docketing an appeal or filing a petition for a writ of certiorari in the above-entitled case be, and the same is hereby, extended to and including January 21, 1982.

/s/ Byron R. White
Associate Justice of the Supreme
Court of the United States

Dated this 11th
day of December, 1981.

APPENDIX H

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Constitution of the United States, Article I, Section 10, Clause 1:

> No State shall . . . pass any . . . Law impairing the Obligation of Contracts . . . .

Sections 102(a) and (b) and 105(a), (b)(1) and (b)(2) of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3312(a) and (b), 3315(a), (b)(1) and (b)(2) (Supp. IV 1980):

> § 3312. Ceiling price for new natural gas and certain natural gas produced from the Outer Continental Shelf
>
> (a) Application
>
> The maximum lawful price computed under subsection (b) of this section shall apply to any first sale of natural gas delivered during any month in the case of—
>
> (1) new natural gas; and
>
> (2) natural gas produced from any old lease on the Outer Continental Shelf and qualifying under subsection (d) of this section for the new natural gas ceiling price.
>
> (b) Maximum lawful price
>
> The maximum lawful price under this section for any month shall be—
>
> (1) $1.75 per million Btu's, in the case of April 1977; and
>
> (2) in the case of any month thereafter, the maximum lawful price, per million Btu's, pre-

scribed under this subsection for the preceding month multiplied by the monthly equivalent of a factor equal to the sum of —

(A) the annual inflation adjustment factor applicable for such month; plus

(B) (i) .035, in the case of any month beginning before April 20, 1981; or

(ii) .04, in the case of any month beginning after April 20, 1981.

* * * *

(Pub. L. 95-621, title I, § 102, Nov. 9, 1978, 92 Stat. 3358.)

§ 3315. Ceiling price for sales under existing intrastate contracts

(a) Application

The maximum lawful price computed under subsection (b) of this section shall apply to any first sale of natural gas delivered during any month in the case of natural gas, sold under any existing contract or any successor to an existing contract, which was not committed or dedicated to interstate commerce on November 8, 1978.

(b) Maximum lawful price

(1) General rule

Subject to paragraphs (2) and (3), the maximum lawful price under this section shall be the lower of—

(A) the price under the terms of the existing contract, to which such natural gas was subject on November 9, 1978, as such contract was in effect on such date; or

(B) the maximum lawful price, per million Btu's, computed for such month under

section 3312 of this title (relating to new natural gas).

(2) Contract price exceeding new gas ceiling price on November 9, 1978

In the case of any natural gas described in subsection (a) of this section for which the contract price applicable on November 9, 1978, exceeds the maximum lawful price, per million Btu's, computed for such date under section 3312 of this title (relating to new natural gas), the maximum lawful price under this section shall be the higher of—

(A) the maximum lawful price, per million Btu's, computed for such month under section 3312 of this title; or

(B) (i) the cont[r]act price on November 9, 1978, in the case of November, 1978; and

(ii) in the case of any month thereafter, the maximum lawful price, per million Btu's, prescribed under this subparagraph for the preceding month multiplied by the monthly equivalent of the annual inflation adjustment factor applicable for such month.

* * * *

(Pub. L. 95-621, title I, § 105, Nov. 9, 1978, 92 Stat. 3363.)

The Kansas Natural Gas Price Protection Act, Kan. Stat. Ann. §§ 55-1401 through 55-1415 (Supp. 1980):

55-1401. Citation of act. This act may be cited as the "Kansas natural gas price protection act."

History: L. 1979, ch. 171, § 1; May 29.

55-1402. Definitions. For the purposes of this act:

(a) "Commission" means the state corporation commission.

(b) "Gas purchase contract" means any contract under which natural gas is sold within the state of Kansas (1) to any person for resale by such person or (2) to any person for use by such person, but shall not be deemed to include rate schedules, contracts or service agreements under which natural gas is sold (i) by a natural gas public utility as defined in K.S.A. 1979 Supp. 66-104, either to a person for use by such person or to a person for resale by such person, which sale is subject to the regulatory jurisdiction of the commission, or (ii) to the ultimate consumers by other persons which are local distribution companies.

(c) "Indefinite price escalator clause" means any provision of a gas purchase contract which provides for the establishment or adjustment of the price of natural gas delivered under such contract by reference to other prices for natural gas, for crude oil, or for refined petroleum products.

(d) "New well" means any well:

(1) The surface drilling of which began on or after February 19, 1977; or

(2) the depth of which was increased, by means of drilling on or after February 19, 1977, to a completion location at least one thousand (1,000) feet below the depth of the deepest completion location such well attained before February 19, 1977.

(e) "New reservoir" means any reservoir that qualifies as a new onshore reservoir under section 102 of the natural gas policy act of 1978.

(f) "Stripper well" means any well qualifying as such under section 108(b) of the natural gas policy act of 1978.

(g) "Price" as used herein means the price for natural gas prior to the assessment of any produc-

tion and conservation fees and taxes by the state of Kansas.

(h) "Committed or dedicated to interstate commerce", when used with respect to natural gas, means natural gas which qualifies as committed or dedicated to interstate commerce under section 2(18) of the natural gas policy act of 1978.

(i) "Person" means (1) any individual, corporation (including cooperatives), public trust or authority, partnership, joint venture or other form of business entity, or voluntary association, or (2) the United States, any state, or any political subdivision, agency or instrumentality of the foregoing.

History: L. 1979, ch. 171, § 2; May 29.

55-1403. Applicability of act to natural gas purchase contracts. Only natural gas purchase contracts entered into before April 20, 1977, providing for the sale, within this state, of natural gas produced in this state and not committed or dedicated to interstate commerce on November 8, 1978, shall be subject to the provisions of this act.

History: L. 1979, ch. 171, § 3; May 29.

55-1404. Effect of indefinite price escalator clauses of certain natural gas purchase contracts on price of natural gas. Except to the extent provided in K.S.A. 1979 Supp. 55-1405 and 55-1406, on or after December 1, 1978, the price allowed to be paid pursuant to federal legislation or any regulation by an agency implementing such legislation, or the price paid or to be paid for any sale of natural gas in the state of Kansas shall not be taken into account in applying any indefinite price escalator clause contained in any gas purchase contract subject to this act, to the extent that such contract provides for the sale in the state of Kansas, of gas produced within

this state which was not committed or dedicated to interstate commerce on November 8, 1978. This section shall not require a reduction of any price contained in any gas purchase contract subject to this act below the price actually paid prior to the date of enactment of this act.

History: L. 1979, ch. 171, § 4; May 29.

55-1405. Same; limited effect of indefinite escalator clauses; price calculated monthly; exceptions. Notwithstanding the restriction on the operation of indefinite price escalator clauses imposed by K.S.A. 1979 Supp. 55-1404, after March 1, 1979, such indefinite price escalator clauses in gas purchase contracts subject to this act may be given effect in accordance with their terms to the extent that the price payable under such contracts is not increased above the maximum price such gas would receive if it qualified under section 109(b) of the natural gas policy act of 1978. The maximum price shall be calculated on a monthly basis. Nothing in this section shall be construed to apply to gas produced from new wells, new reservoirs or stripper wells as defined by this act.

History: L. 1979, ch. 171, § 5; May 29.

55-1406. Same; effect of indefinite price escalator clauses on gas produced from new wells or reservoirs and stripper wells; price calculated monthly; category determinations. Notwithstanding the restriction on operation of indefinite price escalator clauses in gas purchase contracts imposed by K.S.A. 1979 Supp. 55-1404 and 55-1405, after March 1, 1979, with respect to natural gas which is subject to this act, and which qualifies as gas produced from new wells, new reservoirs or stripper wells as defined in this act, such indefinite price escalator clauses may be given effect in accordance with their terms to the ex-

tent that the price payable under such contracts is not increased above the maximum price such gas would receive if it had been committed or dedicated to interstate commerce. The maximum price shall be calculated on a monthly basis. If the parties to the contract cannot agree as to the category of gas for which such gas qualifies under the terms of the natural gas policy act of 1978, then such category determination shall be made by the commission.

History: L. 1979, ch. 171, § 6; May 29.

55-1407. Recovery of productions and conservator fees and taxes. For purposes of this act, the price collected for the first sale of natural gas shall be permitted to exceed any maximum price established by such sections of this act, to the extent necessary to recover any production and conservation fees and taxes attributable to such natural gas.

History: L. 1979, ch. 171, § 7; May 29.

55-1408. Voluntary renegotiation of price provisions. Nothing contained in this act shall prevent or limit the voluntary renegotiation of price provisions contained in natural gas purchase contracts.

History: L. 1979, ch. 171, § 8; May 29.

55-1409. Enforcement of act by commission; rules and regulations. Jurisdiction to implement and enforce the provisions of this act is hereby conferred on the commission, except that nothing in such sections of this act shall be construed to divest the district courts of Kansas of jurisdiction to determine issues relating to private contract rights. The commission may adopt such rules and regulations to implement and enforce this act, as it deems necessary and proper.

History: L. 1979, ch. 171, § 9; May 29.

55-1410. Appellate jurisdiction of supreme court. Appellate jurisdiction is hereby conferred upon the supreme court of this state to review the orders of the commission made under this act. Such appeal may be taken by any person shown by the record to be interested therein, in the same manner and time as appeals are allowed by law to the court of appeals from orders of the commission which relate to rate hearings.

History: L. 1979, ch. 171, § 10; May 29.

55-1411. Price limitations to terminate December 31, 1984; reports by commission; end-use allocation by commission, when. All price limitations as defined in this act shall terminate not later than December 31, 1984. The commission shall monitor and report to the legislature at the commencement of each regular session in each year this act remains in operation, the effect of this act upon the availability of natural gas in this state. In any case where the commission finds that natural gas subject to this act has been or is being diverted to the interstate market, it shall require that the quantity of natural gas which is the object of any other sale of natural gas subject to this act for use as boiler fuel to generate electricity, except for the use thereof for such purpose by municipal utilities and rural electric cooperatives, be reduced in an amount equal to the natural gas so diverted, and that such amount of natural gas be allocated for other uses.

History: L. 1979, ch. 171, § 11; May 29.

55-1412. Credit of gross profits of emergency or spot sales of natural gas in interstate commerce to customers; duties of commission. The commission by appropriate action shall prescribe a method by which the gross profits, including transportation charges,

derived from sales of natural gas produced in this state and sold in interstate commerce pursuant to section 2.68 of the general policy and interpretations of the federal energy regulatory commission or section 311 of the natural gas policy act of 1978, or under any similar statutory or regulatory provisions subsequently adopted, by public utilities including pipelines subject to the jurisdiction of the commission, or subsidiaries or affiliates of such utilities, are credited against the bills of such utilities' customers located within this state. If such a credit is not already being applied by any such utility, the commission shall require that this be commenced within one hundred twenty (120) days from the effective date of this act.

History: L. 1979, ch. 171, § 12; May 29.

55-1413. Certain natural gas distributors to apportion the savings accrued from the operation of this act to its customers. In any case where a natural gas distributor receives both intrastate and interstate natural gas for its system, the commission, by order, shall require any said distributor to apportion the amount of money saved in the purchase of natural gas from the restrictions made by this act on the effect of indefinite price escalator clauses to every customer of such distributor without regard to their source of supply of natural gas.

History: L. 1979, ch. 171, § 13; May 29.

55-1414. Profits of pipelines from certain natural gas sales apportioned to customers. Any intrastate pipeline making an intrastate sale of natural gas the purpose for which is to allow intrastate natural gas to be substituted for interstate natural gas in the compressor facilities of an interstate pipeline shall apportion the profit accrued from such sale to

its natural gas customers without regard to their source of supply.

History: L. 1979, ch. 171, § 14; May 29.

55-1415. Invalidity of part. If any sentence, clause, subsection, or section of this act is held unconstitutional or invalid by any court of competent jurisdiction it shall be conclusively presumed that the legislature would have enacted the remainder of the act not so held unconstitutional or invalid.

History: L. 1979, ch. 171, § 15; May 29.

APPENDIX I

EXCERPTS FROM CONTRACT PROVISIONS

Section 6 of the Gas Purchase Contract (§ 8 of the Residue Gas Contract): *

6 [8]. *PRICE*

6.1 [8.1] During the first Contract Year BUYER agrees to pay SELLER one dollar and fifty cents ($1.50) per MCF for all gas delivered to BUYER at the point of delivery, subject to the BTU adjustment provisions contained herein. At the beginning of the second and each succeeding Contract Year, this price shall escalate two cents (2¢) per MCF, except for those years when the price is redetermined in excess of the two cents (2¢) per MCF escalation.

* * * *

6.7 [8.5] If any federal or Kansas regulatory or governmental authority having jurisdiction in the premises shall at any time hereafter fix a price per MCF applicable to any natural gas of any vintage produced in Kansas, higher than the contract price then in effect under this gas contract, the price to be paid for gas thereafter shall be increased to equal such regulated price. In that event, the increased price shall be effective as of the date of action of the governmental or regulatory authority establishing the regulated price, or its effective date, whichever is later, subject to the provisions of Section 8 [Section 10] hereof.

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* The provisions of the two contracts are identical except for their numbering. The correct paragraph number of the Residue Gas Contract will be indicated in brackets.

Section 7 of the Gas Purchase Contract (§ 9 of the Residue Gas Contract):

7 [9]. *PRICE REDETERMINATION*

7.1 [9.1] SELLER shall have the option to cause the price being paid for its gas by BUYER to be redetermined every two years, beginning in 1977. The request for a price redetermination shall be given in writing by SELLER to BUYER not later than 120 days prior to the beginning of the Contract Year for which the price redetermination is requested. Should such request not be given within the required time, SELLER shall be deemed to have waived its option for that two-year period only. The effective date of any price established by price redetermination shall be the beginning of the Contract Year, subject however, to the provisions of Section 8 [Section 10] hereof.

7.2 [9.2] Within the same one hundred twenty (120) days following SELLER'S request for a price redetermination, the parties shall mutually redetermine the price by considering three (3) contracts under which the highest prices are actually being paid for flowing gas ninety (90) days prior to the date the redetermined price is to be effective. The contracts to be considered shall, (a) have a primary term of one (1) or more years, (b) be for gas produced in Kansas, (c) be for gas purchased by an interstate or intrastate company selling or using an average daily volume of 5,000 MCF or more of gas for the twelve (12) months period ending ninety (90) days prior to the date the redetermined price is to be effective, (d) not be for the purchase of Spivey-Grabs Field gas by BUYER under contracts dated in 1975, (e) not include more than one contract of any one purchaser in any one field, and (f) not be for a price then subject to regulatory suspense or

refunds. In determining the "highest prices" being paid, and as they may apply to a fair market price under this gas contract, BUYER and SELLER shall make valid adjustments in pricing considerations, including but not limited to the heating value of the gas, and costs of gathering, compression and processing rights.

After the BUYER and SELLER have decided on the three contracts and appropriate prices to be used from each one for this redetermination, the weighted average price per MCF being paid under the three contracts shall be calculated. This price shall become the redetermined price to be paid by BUYER to SELLER.

7.3 [9.3] It is agreed that the parties shall have the full one hundred twenty (120) days to reach voluntary agreement on the redetermined price. However, at any time after negotiations have been in process more than sixty (60) days but less than one hundred twenty (120) days, either party may request in writing that the matter be submitted to arbitration as provided in Section 16 [Section 18]—ARBITRATION.

In the event the redetermined price is established by arbitration under Section 16 [Section 18], such redeterminated price shall be effective on the date the board renders its decision, or on the date the redetermined price was to become effective, whichever date is later, subject however, to the provisions of Section 8 [Section 10] hereof.

7.4 [9.4] In no event shall the redetermined price for a contract period be less than the price paid during the previous Contract Year, plus the annual two cents (2¢) per MCF escalation provided above.

Section 8 of the Gas Purchase Contract (§ 10 of the Residue Gas Contract):

8 [10]. *COMMISSION APPROVAL*

8.1 [10.1] BUYER shall have no obligation to pay any increase in prices pursuant to provisions for escalation (Section 6.1) [Section 8.1] for Price Redetermination (Section 7) [Section 9], or for governmental price regulation (Section 6.7) [Section 8.5] until the effective date of the pass-on thereof as authorized by the Kansas Corporation Commission, except as hereinafter provided.

8.2 [10.2] BUYER shall make application to the Kansas Corporation Commission for approval of the pass-on of any of such increased costs of gas not later than sixty (60) days prior to the date the applicable increase is scheduled to become effective, or within five days after the increase has been established by arbitration or by action of governmental or regulatory authorities. The failure of the Kansas Corporation Commission to approve a pass-on within sixty days after application by BUYER shall be deemed a rejection of the price increase for the purposes of this gas contract.

8.3 [10.3] BUYER shall have the option, to be exercised by written notice to SELLER not later than fifteen (15) days after the Kansas Corporation Commission shall have rejected any such pass-on, to pay the increased price and in such event the provisions of this gas contract shall remain in effect. If BUYER does not elect to pay such increase then SELLER shall have the option to terminate this gas contract on thirty days prior written notice.

Section 18 of the Gas Purchase Contract (§ 20 of the Residue Gas Contract):

18 [20]. *GOVERNMENT REGULATIONS*

18.1 [20.1] This gas contract shall be subject to all relevant present and future state and federal laws,

decisions of any courts of law and equity, and all rules, regulations, and orders of any regulatory authority having jurisdiction. Neither party shall be held in default for failure to perform hereunder if such failure is due to compliance with such laws, decisions, rules, regulations, or orders. This section will not operate to affect the rights and options granted to either party as provided for in Section 8 [Section 10] of this gas contract.

Section 23 of the Gas Purchase Contract (§ 25 of the Residue Gas Contract):

23 [25]. *INTENT*

23.1 [25.1] It is the intention of the parties that the price adjustment provisions contained herein are solely for the purpose of compensating SELLER for the anticipated increase in its operating costs and for the anticipated increase in the value of its Natural Gas to be sold hereunder. It is understood that no price escalation, price redetermination or other pricing provision of this gas contract is for the purpose of offsetting any potential increase in SELLER'S Federal income tax liability as a result of the repeal of percentage depletion.

APPENDIX J

May 14, 1979

COMMITTEE REPORT

TO: The Senate and House of Representatives of the State of Kansas

FROM: Special Committee on Energy and Natural Resources

Subject Matter of 1979 H.B. 2680—Restriction of the Operation of Indefinite Price Escalator Clauses in Certain Gas Purchase Contracts

Background

At its meeting of May 4, 1979, the Legislative Coordinating Council appointed the Special Committee on Energy and Natural Resources. The Committee was composed of all members of the standing Committees on Energy and Natural Resources of the Senate and House of Representatives. In accord with the Legislative Coordinating Council directive, the chairperson of each such standing committee served as co-chairperson of the special committee.

The Committee was authorized to meet any time during the period May 7-14 and was directed to study the subject of 1979 H.B. 2680 and to submit its report and recommendation to the Senate and House of Representatives.

In accord with its directive, the Committee met on May 9-11 and 14. Two and one-half days of hearings were held, during which time all persons or groups who desired to do so were given an opportunity to express their views on the subject of study. (A listing of the conferees is included as Attachment I to this report.)

Purpose of H.B. 2680

H.B. 2680, which is similar to a bill enacted in 1979 by the Oklahoma Legislature, represents a limited exercise by the State of Kansas of the power reserved to the states by the federal Natural Gas Policy Act of 1976 (NGPA) to set certain maximum prices for the first sale of natural gas produced within the state in the intrastate market. The bill is designed to affect *only* certain of the natural gas purchase contracts which were entered into before April 20, 1977, and which provided for the intrastate sale of natural gas not committed on November 8, 1978, to interstate commerce. Specifically, the bill would restrict the operation of indefinite price escalator clauses in gas purchase contracts containing such clauses. Indefinite price escalator clauses are of several varieties, but they all provide for some indeterminent future price increases which are beyond the control of the contracting parties. For example, "triggering" of price increases might result from inflation rates, by the highest price paid by the purchaser to other producers, by the highest price received within a specified geographic area, by the highest price allowed to be paid by a federal or state regulatory agency, etc.

H.B. 2680 is designed to prevent indefinite price escalator clauses in gas purchase contracts covered by the bill, on and after December 1, 1978, from triggering because of the ceiling prices established in the NGPA or because of the actual payment of those prices. Price escalation would be permitted under the bill, but it would be in accord with the levels established in Sec. 109 of the NGPA. That section refers mainly to gas that commonly has been described as "old interstate" natural gas. As of April 1979, the ceiling price for such gas was $1.672 *

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* Since prices paid by the ultimate consumer may be reflective of a variety of different gas contract prices and consumer price controls, it should not be assumed that any individual consumer's costs would necessarily reflect the full amount of the differences in prices herein described.

per MMBTU. This ceiling price is permitted to increase each month in accord with an inflation factor.

There was general agreement among those who appeared before the Committee that if no legislation were passed, the price of intrastate natural gas in many of the contracts having indefinite price escalator clauses would increase to the ceiling price set in NGPA for new natural gas (Sec. 102). The ceiling price for such gas as of April, 1979, was $2.156* per MMBTU. The price for this category of gas is subject to monthly changes based on an inflation adjustment factor and a real growth factor.

The restraints on old intrastate gas prices under the contracts affected by H.B. 2680 would cease to be effective after December 1, 1984.

In summary, due to the changes in the gas pricing system brought about by NGPA, H.B. 2680 would have the effect of restricting somewhat abrupt and unanticipated increases in the price of old gas dedicated to intrastate commerce under certain gas purchase contracts which contain indefinite price escalator clauses.

In 1978, a total of 866.6 billion cubic feet (BCF) was *produced* in Kansas. Approximately 731.6 BCF was dedicated to the interstate market, while 135.0 BCF went to the intrastate market. Of the latter amount, approximately 50.0 BCF was gas subject to indefinite price escalator clauses likely to be affected by the provisions of H.B. 2680. In 1975, the total consumption of gas in Kansas was 566.6 BCF of which 293.7 BCF was supplied within Kansas. Gas is used by residential, commercial and industrial customers.

An estimate provided by the major Kansas intrastate natural gas suppliers is that the increased cost to consumers, if H.B. 2680 is not passed, would be about $16.5 million in 1979 and an estimated $127.5 million during the operative life of this measure. These figures were not

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* [See footnote on p. 72a.]

disputed by any of the conferees. Obviously, the increase would be smaller if the bill is enacted.

Pros and Cons

Extensive oral and written testimony was received by the Committee. This information is available in the office of the Director of Legislative Administrative Services. Rather than to attempt to summarize this testimony, much of which is technical and detailed, the Committee elected to glean from the information the main arguments presented by both the proponents and opponents. The Committee believes this form of presentation will be most helpful to the members of the Legislature in their consideration today of the issues presented in the bill.

For H.B. 2680. The NGPA of 1978 marked a radical reversal of the federal policy toward the pricing of natural gas. This law is directed toward increasing the price of gas, with the ultimate goal of deregulation of gas pricing. For many years, federal policy was directed toward pricing gas on a cost of service basis in interstate commerce. The new policy is to establish ceiling prices which will rise monthly to the point of final deregulation of many categories of natural gas production on December 31, 1984.

Proponents believe that as a result of this legislation, many producers of natural gas, especially those whose contracts contain indefinite price escalator clauses, will reap unanticipated, windfall financial benefits. These benefits bear no real relationship to the cost of production of new gas, and are not even remotely related to old gas production costs. They accrue solely because of the reversal of the federal policy.

The proponents stated that the burden of the increased gas costs will be passed by the utility companies directly to the consumer. The producers will benefit beyond any expectations they might have had only a few years ago

and the consumers, already buffeted by rapidly increasing inflation, including spiraling utility costs, will pay. Natural gas prices will continue to increase in the forseeable future.

The Congress recognized this scenario and, as a result, specifically reserved to the states an area of price control applicable to intrastate gas sales, according to proponents.

The proponents contended that H.B. 2680 represents an effort by the State of Kansas to minimize the impact on consumers of natural gas price increases of some intrastate gas from the present time through 1984. For a period of nearly six years, this bill would provide a modicum of restraint on some utility price increases.

Against H.B. 2680. According to opponents, the bill is designed to discriminate against a select group of gas producers—those whose production is in the intrastate market and whose old gas contracts contain indefinite price escalator clauses—and to spread the benefit of such discrimination among only a relatively few consumers scattered unevenly throughout the state.

Opponents argued that passage of the bill would result in the diversion by producers of natural gas from the intrastate to the interstate market. This means that more Kansas gas will be denied to Kansas consumers and made available to consumers in the populous northeastern United States. This will occur because producers, when the choice is available, would cancel existing contracts and sell their gas into interstate systems where higher prices are available. This represents a complete reversal of the previous pattern in which the intrastate market was more lucrative to the producers than the interstate market.

Since the bill would reduce the prices that producers may receive for old intrastate gas under contracts with indefinite price escalators, opponents believe that

capital dedicated to exploration will be diverted, in some cases, to areas that appear more economically attractive, *e.g.*, to states having some congenial pricing environments or to areas more easily accessible to interstate markets. In addition, operation of some marginal producing wells will be discontinued earlier than otherwise would occur because the lower gas prices will cause their operation to become uneconomical sooner.

Opponents stated that the bill represents yet another attempt by government, state government in this case, to impose regulations on the natural gas industry. Federal regulation, for too long, kept prices for natural gas in interstate commerce at artificially low levels. Just when the Congress has recognized the folly of that policy by enactment of NGPA, it appears that Kansas might deliberately adopt a policy applicable to the intrastate market not unlike that just discarded at the federal level for the interstate market. Producers can be expected to avoid intrastate marketing in a state market that is clouded by the uncertainty of a diverse and unpredictable governmental regulation.

The bill would represent modification by the state of the pricing provisions of existing gas purchase contracts. Opponents believe this action might be construed as violation of the protection of contracts afforded by the U.S. Constitution and raises several state and federal constitutional questions.

Also, according to the opponents, some gas producers would incur an additional economic loss in instances where the oil and gas lease terms provide for the computation of gas royalty proceeds on a market value rather than sales proceeds basis.

Conclusions and Recommendations

Simply put, based on April 1979 data, the price of the intrastate gas affected by H.B. 2680 would be $1.672 per MMBTU as compared with $2.156 MMBTU without the

bill, a 29 percent savings. Over time, the gap between these two prices will increase. This savings to consumers is ample reason to support the passage of H.B. 2680.

Furthermore, as a result of its hearings and deliberations, the majority of the Committee is strongly convinced that the single issue of the benefits to be derived by the affected Kansas consumers of natural gas clearly outweights [sic] any adverse effects the gas producers or royalty owners said the bill might have. Based on its analysis of the NGPA and various legal opinions, the Committee also believes that the producers' argument regarding impairment of contracts is without merit. Except where long-term, fixed price contracts are involved, the producers and royalty owners are benefiting significantly under the new NPGA. The bill merely prevents the producers' from receiving the full amount of unanticipated gains that would be experienced. In conclusion, the Committee determination is that the Bill will have neither a substantial negative impact on (a) the availability of intrastate gas, nor (b) the future exploration activities of natural gas producers.

It should be noted that the Committee did not consider any amendments to the bill. No conferee offered the Committee any amendment to the bill.

The Committee, by a 17-15 vote, recommends that H.B. 2680 be passed, without amendment, by the Kansas Senate.

Signed,

/s/ Charlie Angell
Senator CHARLIE ANGELL,
Co-Chairperson

/s/ Robert H. Miller
Representative ROBERT MILLER,
Co-Chairperson

Representative James Cubit
Representative Keith Farrar
Representative August Bogina
Representative Don Crumbaker
Representative Victor Elliott
Representative Ben Foster
Representative James Gillmore
Representative Francis Gordon
Representative R. D. McCrum
Representative John Sullivan
Representative J. E. Talley
Representative Don Mainey
Representative Richard Brewster
Representative George Dean
Representative Anita Niles
Representative Irving Niles
Representative Jack Rodrock
Representative Fred Rosenau
Representative Jack Shriver
Representative John Solbach
Senator Fred Kerr
Senator Arnold Berman
Senator Paul Feleciano
Senator Richard Gannon
Senator Paul Hess
Senator Jack Janssen
Senator Bill Morris
Senator Larry Rogers
Senator John Simpson
Senator Merrill Werts

ATTACHMENT I

Richard C. Loux, Chairman, Kansas Corporation Commission

Joe King, Director, Kansas Energy Office

David Black, Vice-President and General Counsel, Kansas Power and Light

Frank Trotman, Southwest Irrigators

Howard Partington, City Administrator, Goddard and Cheney, Kansas

Ralph McGee, Kansas AFL-CIO

Bud Grant, Kansas Association of Commerce and Industry

Senator Gene C. Howard, President Pro-Tem, Oklahoma Senate

Art Schnose, Sunflower Electric Cooperative

Donald P. Schnacke, Kansas Independent Oil and Gas Association

R. D. Randall, Petroleum Inc.

Robert Anderson, Mid-Continent Oil and Gas Association

Jim Upchurch, Mesa Petroleum

Darryl Smette, Energy Reserve Group

Byron Thomas, Pickrell Drilling Company

F. W. Mallonee, President, Kansas Independent Oil and Gas Association (KIOGA)

Daley Stucky, Southwest Kansas Royalty Owners

Bob Edmiston, Edmiston Oil

Bill Weiler, Solar Builder

John Roger McCoy, President, McCoy Petroleum Corp.

MINORITY REPORT

We, the undersigned, disagree with the recommendation of the majority. There are several reasons for our opposition to the recommendation that H.B. 2680, without amendment, be passed by the Kansas Senate.

From the evidence presented to the Committee during two and one-half days of hearings and discussions, one cannot avoid the conclusion that the risks associated with passage of H.B. 2680 far outweigh the benefits a few Kansas consumers might receive in the short term.

These risks involve the consequences that could arise if the Legislature restricts the operation of indefinite price escalator clauses, thereby, in all probability, impairing existing intrastate gas purchase contracts. Those contracts usually contain option clauses allowing for the termination of the contracts if the purchaser refuses to pay the increased prices resulting from the triggering of price escalator clauses. One conferee stated to the Committee that three contracts already had been terminated for that reason.

If any contracts are terminated, it seems inevitable that every effort will be made to divert old intrastate gas into the interstate market where it will receive a higher price. KPL, in its filing with the Kansas Corporation Commission to pass on the increased cost of gas, stated that the failure to pass on those costs could result in the loss of that gas to Kansas. The loss of this old intrastate gas would be permanent. It also is apparent that state-imposed restrictions impairing contracts (by setting a lower ceiling price for old intrastate natural gas than for new gas) will create an unfavorable economic climate for gas producers in Kansas. As described in the majority report, this is a departure in state policy. Kansas has never before regulated the price of gas. Testimony has clearly shown that the incentive of gas producers to explore and develop gas resources in Kansas would be jeopardized.

Our principal concern about H.B. 2680 is whether the benefits that might accrue from passage of the bill would justify taking risks that potentially would have an adverse long-term effect on the Kansas economy.

From the testimony, it became clear that enactment of H.B. 2680 would benefit a relatively small number of Kansas gas users, particularly residential customers. In 1978, Kansas produced 866 billion cubic feet (BCF) of gas. It has been estimated that only 135 BCF of that total constitutes the intrastate market, and further, that only about 50 BCF is under gas purchase contracts with indefinite price escalator clauses. Only intrastate gas purchase contracts containing indefinite price escalator clauses would be affected by H.B. 2680.

The impact that would result from the passage of H.B. 2680 would increase the inequality between intrastate and interstate prices paid by Kansas consumers. The following figures reveal the price increases that will result from the Natural Gas Policy Act of 1978 (NGPA) on both interstate and intrastate gas:

Service Area *	Price Before NGPA	Price After NGPA
Area A (intrastate gas)	$1.25	$1.39
Area B (interstate gas)	$1.83	$2.03
Area C (interstate gas)	$1.19	$1.49

* Kansas Power and Light Company has three gas service areas. Area A is their mainline system which is supplied solely by intrastate gas. Areas B and C are supplied by interstate gas pipeline companies.

Enactment of H.B. 2680 would only affect Service Area A. Obviously, preventing any price increase in Area A would increase the differences KPL customers in various areas would have to pay for gas. Also, the increased price gas customers would have to pay in Area A is not sufficiently onerous to justify taking the risks that are involved.

From the testimony we found that KPL, the main proponent of the bill, sells approximately 69 percent of

its gas to industrial customers, other utilities, and to itself for use in the generation of electricity. With approximately 37 percent of KPL's gas going to industrial customers, legislation benefiting those industrial customers would give them an unfair advantage over other industrial customers in the state. There also was evidence that a substantial portion of the gas, the price of which would be held down by H.B. 2580 [sic], is used as boiler fuel. More than half the energy value of the gas is lost when it is used as a boiler fuel. We believe that the conservation of natural gas which is a non-renewable premium fuel, must have the highest priority in our state's energy policy. Any effort to limit the price of gas can only continue to encourage inappropriate and inefficient uses of that fuel.

The Committee was informed that in Oklahoma, where legislation similar to H.B. 2680 was enacted, the use of gas for boiler fuel is being encouraged. We take strong exception to such a frivolous and wasteful practice, and we believe that passage of H.B. 2680 in Kansas would be an endorsement of that policy in this state.

Testimony was presented to the Committee on the Oklahoma legislation similar to H.B. 2680. It must be pointed out that there are substantial differences between the gas markets in the two states:

GAS PRODUCTION AND SALES IN OKLAHOMA AND KANSAS* (in BCF)

	Total Sales	Interstate	Intrastate	Percent of Intrastate Gas with Indefinite Price Escalator Clauses	Total BCF in Contracts with Indefinite Price Escalator Clauses
Oklahoma	1,778.2	1,173.4	605.8	65	393
Kansas	866.6	731.6	135.0	37	50

* Oklahoma data are based on sales while Kansas data represents production.

It was reported to the Committee that the estimated first year impact of the triggering of indefinite price escalator clauses caused by NGPA would have been 15 times greater in Oklahoma than in Kansas. One of the authors of the Oklahoma law admitted to the Committee that there could be a drain of gas from Oklahoma because intrastate pipelines are filled to capacity and there is a surplus of intrastate gas in Oklahoma. The same conditions do not prevail in Kansas.

In light of the small savings a limited number of gas consumers would receive in the short run if H.B. 2680 were enacted, we are unwilling to risk the loss of intrastate gas to the interstate markets, and we are unwilling to risk the loss of additional exploration and production in the state which might result from the passage of the bill.

Finally, we are unwilling to run the risk of higher gas prices in the future which could result from the potential loss of intrastate gas that passage of H.B. 2680 could cause.

It appears to us that H.B. 2680 has been designed primarily to support the contention of KPL in its contract dispute with Mesa Petroleum Co. which is presently being litigated in Grant County District Court. The Legislature should not become involved by taking sides in such contract disputes. This is a legal matter appropriately handled by the courts and not by the Legislature.

In our judgment, the Legislature is playing energy roulette with the future energy needs of Kansas citizens. We have grave concern about the long term impact such legislation would have on the people (*i.e.*, consumers) of Kansas.

We believe the people of Kansas, especially the residential consumers, are the victims of a cruel hoax concerning the issue in H.B. 2680. They have been led to

believe that this legislation will freeze or severely check the increases in natural gas costs and related utility rates. The evidence is to the contrary. Only the rate of increase of some rates to some consumers, mostly industrial consumers, would be affected, and then only until 1984. Once this legislation expires, rates will jump to the market place levels. What will have happened to those responsible for this legislation? They will have reaped the short-term benefits of the publicity they have received in recent days, they will have damaged the Kansas economy for the longer term, and they will disavow any of the responsibility for the new "sudden surge" of rates that will occur under the bill which they presently are promoting.

The undersigned also wish to express the most strenuous objection to the procedure employed by the proponents during the Committee deliberation. The parliamentary tactics used effectively precluded the presentation and debate of a number of amendments which we believe are needed if legislation such as H.B. 2680 is to be passed. That bill was literally copied from the Oklahoma law to fit Oklahoma circumstances. It has been amply demonstrated that Kansas conditions are vastly different and that changes in the bill are needed if we legislate in this area. It is evident from the fact that 15 of the members opposed the Committee recommendation that the Committee should have devoted more of its efforts to debate and discussion of the specific provisions of the bill. It should be remembered that a few days ago some of the members of the majority were critical of the fact that the Legislature did not hold hearings on the bill. Now they have successfully foreclosed debate on many of its controversial features.

Summarized below are the amendments the undersigned believe should be considered if the bill is to receive serious consideration:

1. An amendment to delete from the bill reference to gas produced from wells located at a depth of more than 15,000 feet;

2. two technical and clarifying amendments;

3. an amendment which adds to the bill a new section providing for gross profits of Kansas public utilities or pipelines from emergency or spot sales of intrastate natural gas to the interstate market to be credited to the Kansas customers of the utility or pipeline;

4. an amendment which adds to the bill a new section providing for the provisions thereof to be inoperative during any period of time that the Kansas Corporation Commission prohibits new residential hook ups for natural gas service;

5. an amendment to section 11 of the bill providing for the reduction of the amount of natural gas utilized for boiler fuel for the generation of electrictly in an amount equal to natural gas found by the Kansas Corporation Commission to have been diverted from the intrastate to the interstate market;

6. an amendment to section 8 providing that voluntary renegotiation between both parties of price provisions under redetermination procedures be not limited or prevented;

7. an amendment which adds to the bill a new section providing for any natural gas distributor receiving gas at a lower price as a result of the restriction on indefinite escalator clauses made by the bill to apportion to all its Kansas customers the moneys saved; and

8. an amendment which adds to the bill a new section providing for the pass through to the pipeline's customers of any profit accrued by an intrastate pipe-

line in making any sale of intrastate gas to be substituted for interstate gas in compressor facilities of an interstate pipeline.

These proposed amendments are designed to strengthen the bill for Kansas consumers, "Kansasize" the Oklahoma version's idiosyncrasises, and insure that public utilities and pipelines are prohibited from certain practices. Adoption of these amendments would make the measure better, but certainly do not alleviate all objections to the bill.

Joint Appendix

Office - Supreme Court, U.S.
FILED
JUN 11 1982
ALEXANDER L. STEVAS,
CLERK

No. 81-1370

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

JOINT APPENDIX

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June 12, 1982

APPEAL DOCKETED JANUARY 21, 1982
PROBABLE JURISDICTION NOTED MARCH 29, 1982

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1370

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

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The following opinions, orders, journal entries, legislative reports, and relevant constitutional, statutory, and contract provisions have been omitted in printing this appendix because they appear on the following pages in the printed appendix to appellant's Jurisdictional Statement, filed on January 21, 1982:	
Opinion of the Supreme Court of Kansas, July 17, 1981, reported at 230 Kan. 176, 630 P.2d 1142 (1981)	1a
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Special Comm. on Energy & Natural Resources, *Report on 1979 H.B. 2680—Restriction of the Operation of Indefinite Price Escalator Clauses in Certain Gas Purchase Contracts* (1979) 71a

DISTRICT COURT FOR
HARPER COUNTY, KANSAS

Civ. No. 79-37

ENERGY RESERVE GROUP, INC.,
Plaintiff,

v.

THE KANSAS POWER & LIGHT CO.,
Defendant.

DOCKET ENTRIES *

DATE	PROCEEDINGS
1979	
July 2	Petition filed by Pl.; Action docketed; Summons issued to Sheriff for service on agent for Def.
July 19	Answer and Counterclaim filed by Def.
Aug 20	Answer to Def's. Counterclaim and amended Petition filed by Pl.
Sept 4	Answer to Pl's. Amended Petition and Counterclaim filed by Def.
Nov 30	Motion for Summary Judgment filed by Pl., together with supporting Memorandum.
Dec 24	Cross-Motion for Summary Judgment filed by Def., together with Suggestions in Support.
1980	
Feb 4	Pl's. Memorandum opposing Def's. Cross-Motion for Summary Judgment, together with Appendix and Affidavits.

* Entries deemed irrelevant by the parties have been omitted.

DATE	PROCEEDINGS
1980	
Feb 20	Def's. Reply Brief in support of its Cross-Motion for Summary Judgment; Def's. Statement of Uncontroverted Facts; Motion for Leave to File Responses or, in the Alternative, to Strike Portions of Pl's. Memoranda & Supporting Affidavits filed by Def., together with Suggestions in Support.
March 7	Pl's. Response to Def's. Proposed Statement of Uncontroverted Facts.
March 27	Def's. Responses to and Statements of Uncontroverted Facts and Position on Pl's. two Claims of Breach of Contract Based on Stripper Well Gas.
April 15	Memorandum Opinion, denying Pl's. Motion for Summary Judgment and sustaining Def's. Cross-Motion for Summary Judgment and for declaring judgment.
April 23	Pl's. Motion to Reconsider and Alter and Amend Judgment.
May 21	Pl's. Memorandum in Support of Motion to Reconsider and to Alter and Amend Judgment.
June 10	Def's. Response to Pl's. Memorandum in Support of Motion to Reconsider and to Alter and Amend Judgment.
July 14	Memorandum Opinion, denying Pl's. Motion to Reconsider and to Alter and Amend Judgment.
Oct 2	Journal Entry, overruling Pl's. Motion to Reconsider and to Alter and Amend Judgment.
Oct 30	Notice of Appeal filed by Pl.

SUPREME COURT OF THE
STATE OF KANSAS

No. 80-52677-AS

ENERGY RESERVE GROUP, INC.,
Appellant,

v.

THE KANSAS POWER & LIGHT CO.,
Appellee.

DOCKET ENTRIES *

DATE	PROCEEDINGS
1980	
Nov 4	Notice of Appeal to the Kansas Court of Appeals; Motion to Transfer to the Supreme Court and to Consolidate with 80-52646-A filed by Appellee.
Nov 12	Appellant's Suggestions in Support of Appellee's Motion to Transfer and in Opposition to Appellee's Motion to Consolidate.
Nov 19	Appellee's Reply Suggestions in Support of Motion to Consolidate.
Dec 9	Order transferring case to the Supreme Court and denying motion to consolidate.
1981	
Jan 14	Order granting permission for the Kansas Independent Oil and Gas Association to file a Brief *Amicus Curiae.*

* Entries deemed irrelevant by the parties have been omitted.

DATE	PROCEEDINGS
1981	
Feb 4	Order granting permission for the Kansas Corporation Commission to file a Brief *Amicus Curiae*.
Feb 9	Brief filed by Appellant.
Feb 13	Brief *Amicus Curiae* filed by the Kansas Independent Oil and Gas Association.
March 3	Brief filed by Appellee.
March 4	Brief *Amicus Curiae* filed by the Kansas Corporation Commission.
March 30	Reply Brief filed by Appellant.
July 17	Judgment entered affirming judgment of the District Court; Mandate issued.
Aug 6	Motion for Rehearing filed by Appellant.
Aug 13	Brief in Opposition to Motion for Rehearing filed by Appellee.
Sept 23	Order denying Motion for Rehearing.
Dec 8	Notice of Appeal to the United States Supreme Court filed by Appellant.
1982	
April 1	Order of the United States Supreme Court noting probable jurisdiction.

BEFORE THE
STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Before Commissioners: Richard C. (Pete) Loux,
Chairman
Jane T. Roy
William G. Gray

Docket No. 118,447-U

IN THE MATTER OF THE APPLICATION OF THE KANSAS POWER & LIGHT COMPANY FOR AUTHORITY TO ADJUST ITS RATES FOR NATURAL GAS SALES IN AMOUNTS SUFFICIENT TO OFFSET CHANGES IN ITS WHOLESALE COST OF GAS.

ORDER

Now, on this 9th day of November, 1979, the above-entitled matter comes on for consideration and decision before the State Corporation Commission of the State of Kansas before Commissioners Richard C. (Pete) Loux, Chairman; Jane T. Roy; and William G. Gray.

This matter comes on for decision as a result of the application as supplemented by The Kansas Power & Light Company (Applicant) for authority to adjust its rates for natural gas sales in amounts sufficient to offset changes in its wholesale cost of gas.

This matter was originally heard by the Commission on May 2, 1979. At that hearing the Applicant was represented by David S. Black and James L. Grimes of Topeka, Kansas. Curtis M. Irby, Assistant General Counsel, State Corporation Commission, appeared on behalf of the Commission's staff and public generally.

The Commission having taken this matter under advisement, having reviewed its files and records finds and concludes as follows:

1. That notice in this matter was proper and that it complied with both the laws of the State of Kansas and the rules and regulations of the State Corporation Commission.

2. That on December 7, 1978, the Applicant filed an application with the Commission in which it sought authority to recover any increase costs of purchased gas on its main system which might be occasioned by the activation or "triggering" of certain indefinite price escalator clauses contained in its gas purchase contract as a consequence of the passage by the Congress of the United States of the Natural Gas Policy Act (NGPA), of 1978.

3. On February 2, 1979, the Applicant filed a supplemental application with this Commission stating that it had received a demand from one of its principal natural gas suppliers (Mesa) for the payment of higher prices for the gas purchased by KP&L under such contract because of the alleged triggering of the indefinite escalator clause contained in such contract by reason of the enactment of the NGPA.

4. The Applicant in its supplemental application stated that it was its position that the claims of the producer (Mesa) were not well founded and that the Applicant did not owe the sums claimed.

5. The Applicant, however, went on further to state that because a significant portion of its gas reserves were jeopardized by the demands or expected demands of numerous of its gas suppliers under contracts containing similar indefinite escalator clauses, that the Applicant should be authorized by the State Corporation Commission to pass through the claimed increase in purchased gas cost under conditions which would protect the Applicant and its customers pending resolution of the issues between the parties.

6. On May 2, 1979, the application as supplemented came on for hearing before the State Corporation Commission. It is noted here that Harold A. Houske, a Commissioner who was present at the hearing on May 2, 1979, is now deceased and Jane T. Roy has been nominated to fill his vacancy. In the hearings, the Applicant asked for authority to pass on to its customers the increased costs which were reflected in the demands made upon it by several of its producers, and by an amount which reflected increased purchased gas costs under all of its contracts with the natural producers whose contracts contained indefinite escalator clauses and which the producers claim were triggered by the enactment of the NGPA. The Applicant proposed to place the revenues to be received from its customers into an escrow account from which producers would be paid in the event the issues between the Applicant and the producers were ultimately resolved adversely to the Applicant, or from which refunds to its customers would be paid in the event that the issues in controversy were resolved favorably to Kansas Power & Light Company. Interest earned by the funds so deposited would accrue either to the producer if they prevailed or the Applicant's customers upon final resolution of the issues.

7. On May 29, 1979, House Bill 2680 became the law of the State of Kansas. This law known as the Kansas Natural Gas Price Protection Act under the specific terms and conditions set forth therein expressly prevents the triggering of indefinite price escalator clauses in existing intrastate natural gas purchase contracts by the enactment of the Natural Gas Policy Act.

8. Several natural gas producers in the state of Kansas have instituted legal proceedings against the Applicant in the State courts asking for the higher prices and challenging the constitutionality of House Bill 2680.

Additionally the Commission has been sued in the United States District Court for the District of Kansas, challenging the constitutionality of the Kansas Natural Gas Price Protection Act.

9. The Kansas Natural Gas Price Protection Act is the law of the state of Kansas and the Kansas Corporation Commission is charged with responsibility for its enforcement.

10. The claims of the producers who have initiated legal action against both the Applicant and the Commission are in the process of litigation and the date of the resolution of this litigation is not foreseeable by this Commission.

11. The Commission finds itself in a perplexing position. It recognizes the potential contingent liability that the Applicant and its customers might be faced with if this litigation would be resolved adversely to the Applicant. The Commission further would note that the Applicant does not benefit monetarily from either this litigation or the payment of the higher price, but has taken its position in the litigation on behalf of its customers. However, the Commission must enforce the law of the State of Kansas and that law prohibits payment by the Applicant of the prices demanded by the producers.

12. The Commission would further state that in the event that the litigation is determined adversely to the Applicant or that the Kansas Natural Gas Price Protection Act is ultimately declared unconstitutional, then and in that event the Commission would deem it appropriate for the Applicant to request relief from this Commission.

IT IS, THEREFORE, BY THE COMMISSION ORDERED that the application filed herein, and as supplemented, is hereby denied.

The Commission retains jurisdiction of the subject matter and the parties for the purpose of entering such further order or orders as from time it may deem proper and expedient.

Loux, Chmn.; Roy, Com.; Gray, Com.

JAMES B. DOUGLAS
Executive Secretary

CMI:ps

Motion to Dismiss or Affirm

Office - Supreme Court, U.S.
FILED
MAR 8 1982
ALEXANDER L. STEVAS,
CLERK

No. 81-1370

In the Supreme Court of the United States

October Term, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

vs.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF KANSAS

MOTION TO DISMISS

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QUESTIONS PRESENTED

I. Whether the price control provisions of the Kansas Natural Gas Price Protection Act violate the Contract Clause of the United States Constitution when the statute was enacted to further, and in fact furthers, the historically legitimate state goal of controlling intrastate natural gas prices; when the Act contains numerous provisions to limit the severity of its impact on existing contracts; and when the alternative legislative measures proposed by ERG would either increase significantly the prices on old gas in Kansas, without increasing gas supplies, or more severely impair the contracts of gas producers.

II. Whether the "government pricing" clause in ERG's intrastate natural gas supply contracts with KPL provided, based upon Congressional enactment of NGPA price ceilings, a price increase on December 1, 1978.

PARTIES BELOW

Appellee's true and correct name, as reflected in the pleadings below, is The Kansas Power and Light Company. Appellee has no parent corporation, subsidiaries or affiliates.

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No. 81-1370

In the Supreme Court of the United States

October Term, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

vs.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF KANSAS

MOTION TO DISMISS

Appellee The Kansas Power and Light Company ("KPL") moves, pursuant to Supreme Court Rule 16.1(b), for dismissal of this appeal on the ground that it fails to present a substantial federal question.

STATEMENT OF THE CASE

This appeal presents a broad constitutional challenge to intrastate natural gas price control legislation, J.S.App. 58a,[1] which Kansas recently enacted as the intrastate component of, and pursuant to express authorization in, the new federal policy of natural gas pricing embraced by the Natural Gas Policy Act of 1978 ("NGPA").[2] This is one

1. Kansas Natural Gas Price Protection Act, Kan. Stat. Ann. §§ 55-1401 et seq. (Supp. 1980). Citations herein are to the Jurisdictional Statement ("J.S."), the Appendix ("J.S.App."), and the Record on Appeal ("R.Vol.") filed with the Clerk of the Supreme Court.

2. 15 U.S.C. §§ 3301 et seq. (Supp. IV 1980).

in a series of cases filed in Kansas state and federal courts by producers who seek for their old intrastate gas the maximum NGPA new gas incentive price, which Congress established as an intrastate ceiling expressly subject to state authority to impose more stringent controls.

Consistent with its long history of natural gas regulation, Kansas here so exercised that authority both at the request of the state's new governor and with the support of overwhelming majorities in both state legislative houses. The subject Kansas regulations limit price increases available under indefinite price escalator clauses, which traditionally had been regulated under prior Federal law and still are regulated under the NGPA. The Kansas statute limits only the potentially most volatile price increases for intrastate gas in Kansas and reasonably ties those increases to the NGPA price ceilings for comparable gas categories in the interstate market.

Energy Reserves Group, Inc. ("ERG") filed this action for a declaratory judgment that it could and did terminate its two natural gas contracts with KPL. ERG filed this action after KPL refused to pay for ERG's old gas the higher new gas price demanded by ERG, but forbidden by state law. ERG here appeals from an adverse final judgment, J.S.App. 45a, affirmed by the Kansas Supreme Court, J.S.App. 1a, which holds that the statutory price controls constitutionally prohibited the price increases on which ERG's claims of termination were dependent.

A. Enactment of the NGPA

The NGPA is the outgrowth of President Carter's National Energy Plan,[3] announced on April 20, 1977, which

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3. Executive Office of the President, Energy Policy and Planning, *The National Energy Plan* (1977).

set forth a new federal policy of gradual, partial deregulation of natural gas prices. The NGPA sought to increase natural gas supplies while minimizing the unemployment and inflation that higher energy prices produce.[4] The NGPA also addressed a national gas supply allocation problem created by higher intrastate prices that inhibited gas deliveries to the interstate market.[5]

The NGPA embraces a compromise approach to achieve these goals.[6] Representing the resolution of two markedly dissimilar bills,[7] the NGPA increases regulation of intrastate gas, but gradually introduces, to increase gas supplies, higher and ultimately deregulated prices for new production and for continued production from low volume gas sources. Congress expressly found, however, that deregulation of old gas prices would have "little impact on production," but would seriously stimulate inflation and unemployment.[8] The NGPA thus indefinitely continues the regulation of old gas prices as a means of consumer protection.

To implement these objectives, the NGPA abandoned, effective December 1, 1978, the prior practice of admin-

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4. Staff of Subcomm. on Energy and Power of the House Comm. on Interstate and Foreign Commerce, 95th Cong., 2d Sess. *Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978* 2 (Comm. Print 1978) ["Economic Analysis of the NGPA"].

5. *Economic Analysis of the NGPA, supra* note 4, at 10; Executive Office of the President, Energy Policy and Planning, *The National Energy Plan* 52-53 (1977).

6. *See Air Prods. & Chems. Inc. v. FERC*, 650 F.2d 687, 705 & n.25 (5th Cir. 1981).

7. H.R. 8444, 95th Cong., 1st Sess., 123 Cong. Rec. 27187, 27244-45 (1977); S. 2104, 95th Cong., 1st Sess., 123 Cong. Rec. 32306 (1977). The House bill provided for extension of regulations, with increased incentive prices for new gas. H.R. 8444, 95th Cong., 1st Sess. § 401(b)(1) (1977). The Senate bill proposed phase-in deregulation of new gas prices and did not extend controls to intrastate gas. S. 2104, 95th Cong., 1st Sess. §§ 24(a)(5), 24(b)(2) (1977).

8. *Economic Analysis of the NGPA, supra* note 4, at 12, 13.

istrative prescription of interstate natural gas rates based upon cost of production and a reasonable rate of return. 15 U.S.C. § 3431 (Supp. IV 1980). Also effective December 1, 1978, the NGPA established instead "a series of specific statutory maximum price ceilings applicable to discrete types of first sales of natural gas."[9] The NGPA extended these ceiling controls to the intrastate market to encourage a less restricted flow of gas to the interstate market and to non-producing states.

During a six year transition period to substantial deregulation, the NGPA provides, through monthly escalation of these price ceilings, an organized system for the gradual introduction of higher prices for different gas categories. Price incentives designed to increase gas production are drafted into these ceilings. The NGPA provides high price ceilings, together with accelerated monthly escalations, for new gas and new gas production from known reservoirs. The NGPA removes these ceiling restrictions in 1985. Gas from stripper wells with low volume production likewise receives higher incentive price ceilings. 15 U.S.C. §§ 3312, 3313, 3318, 3331 (Supp. IV 1980).

The NGPA, however, does not grant any seller a federal right to any of these ceiling prices. "In no case may a seller receive a higher price than his contract permits."[10] Collection of a higher NGPA price is only permitted "provided that the contract has a sufficient escalation mechanism."[11]

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9. II *Federal Energy Guidelines*, FERC, Stats. and Regs. 30,026.

10. Joint Explanatory Statement of the Comm. on Conference, S. Rep. No. 1126, 95th Cong., 2d Sess. 74 (1978).

11. *Pennzoil Co. v. FERC*, 645 F.2d 360, 375 (5th Cir. 1981), *cert. denied*, 50 U.S.L.W. 3547 (Jan. 11, 1982), quoting H.R. Rep. No. 1752, 95th Cong., 2d Sess. 82 (1978) and 124 Cong. Rec. H13117 (daily ed. Oct. 14, 1978) (statement of Rep. Dingell).

Old intrastate gas not qualified for an incentive price is controlled by NGPA Section 105. 15 U.S.C. § 3315 (Supp. IV 1980). This section controls ERG's contracts. It establishes as the relevant price ceiling the *lower* of the Section 102 new gas price and the "price under the terms of the existing contract . . . as such contract was in effect on [November 9, 1978]." J.S.App. 57a. The Section 105 ceiling, however, is qualified by NGPA Section 602, which provides that states may impose more stringent price controls on intrastate gas. 15 U.S.C. § 3432(a) (Supp. IV 1980). This authority expressly extends to state imposition of restrictions on the "operation of any indefinite price escalator clause" in intrastate contracts.[12] This litigation addresses the Kansas exercise of that authority.

B. Enactment of the Price Protection Act

In its first session after enactment of the NGPA, the Kansas Legislature overwhelmingly enacted the Price Protection Act after serious and lengthy deliberations, including three days of hearings in which numerous gas producers, including ERG, appeared and testified. The Act implemented the policy of state price controls embraced within the NGPA system for regulation of intrastate gas prices.

The Price Protection Act limits natural gas price increases under contractual indefinite price escalator clauses, which otherwise could provide, without regard to market forces,[13] unrestrained price increases in new market con-

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12. Joint Explanatory Statement of the Comm. on Conference, H.R. Rep. No. 1752, 95th Cong., 2d Sess. 125, *reprinted in* [1978] U.S. Code Cong. & Ad. News 9041.

13. "Indefinite escalation clauses 'cause price increases . . . to occur without reference to the circumstances or economics of the particular operation, but solely because of what happens

(Continued on following page)

ditions of escalating price ceilings and partial deregulation under the NGPA. The Act ties escalations for intrastate gas in Kansas to the corresponding NGPA ceiling price for that gas in the interstate market. The Act allows intrastate new gas prices in Kansas to escalate to the Section 102 price for new gas in the interstate market, and the intrastate stripper gas price to escalate to the Section 108 price for stripper gas in the interstate market under the NGPA. Kan. Stat. Ann. § 55-1406, J.S.App. 61a. The Act limits price increases on old intrastate gas in Kansas to the NGPA Section 109 price, which equals the highest NGPA ceiling established for old gas in the interstate market under Section 104. Kan. Stat. Ann. § 55-1405, J.S.App. 61a; see 47 Fed. Reg. 4505 (Feb. 1, 1982) (to be codified in 18 C.F.R. § 271.101).

The Price Protection Act expressly imposed its controls retroactive to December 1, 1978, when the NGPA intrastate price ceiling first became effective subject to state action. The Act thus foreclosed the price increases here claimed by ERG to support its alleged contract terminations.

C. The Decisions Below

This case thus presented to both Courts below the issues of whether ERG's contracts provided for price increases and whether the Price Protection Act could constitutionally limit those price increases.

ERG initially demanded, pursuant to its "government pricing" clause, that KPL pay for all old gas the NGPA

Footnote continued—

under another contract.' . . . There is substantial evidence that in design and function they are 'incompatible with the public interest. . . .'" *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 782-83 (1968).

Section 102 new gas price. This clause triggers an increased price equal to the "higher regulated price" that a governmental authority has "fixed." J.S.App. 66a. Congress allegedly "fixed" the Section 102 price as this "*higher* regulated price," within the meaning of these contacts, when Congress established as a price ceiling for intrastate gas the *lower* of the NGPA Section 102 price and the "price under the terms of [ERG's] contracts."

ERG also claimed the NGPA Section 102 price under its "price redetermination clause", which, on designated dates, adjusts the contract price to the average price under three comparable gas contracts in Kansas. J.S.App. 67a-68a. The parties agreed that this clause would, consistent with NGPA Section 105, trigger a higher price under the terms of ERG's contracts, but for the restrictions of the Kansas Act.

The parties submitted this case on cross-motions for summary judgment on stipulated facts. Both lower courts held that mere enactment of NGPA price ceilings did not trigger a higher price under ERG's government pricing clause. The courts held that the Price Protection Act constitutionally restricted the price increases under the price redetermination clause and forebade the claimed price increase. Because ERG's contracts provided for termination only if the contract price increased and was not paid, the courts declared that the gas supply contracts could not be terminated. J.S.App. 49a.

THE QUESTIONS ARE NOT SUBSTANTIAL

The primary issue presented in this appeal is neither novel nor sufficiently important to warrant this Court's review. The crux of this case is the constitutionality of state legislative price controls on intrastate natural gas.[14] This Court has already affirmed "the power of a state to fix prices at the wellhead on natural gas produced within its borders." *Cities Service Gas Co. v. Peerless Oil & Gas Co.*, 340 U.S. 179, 180 (1950). In numerous contexts this Court has upheld as constitutional state regulation of, and price controls on, intrastate natural gas.[15] Consistent with this Court's contract clause decisions, the Price Protection Act specifically addresses only the most serious source for natural gas price increases, while minimizing its impact on affected producers. The Act does so by limiting indefinite price increases for ERG's gas to a level that ERG did not attempt to challenge below as unreasonable or confiscatory.

ERG here challenges the Price Protection Act as special legislation, which allegedly serves an illegitimate goal of favoritism to KPL, and as allegedly unreasonable legisla-

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14. The second Question Presented is whether the government pricing clause in ERG's contracts provides a price increase in addition to that provided under the price redetermination clause. This is a state law issue for which review in this Court is inappropriate. *See Mesa Petroleum Co. v. The Kansas Power and Light Company*, 229 Kan. 631, 629 P.2d 190, *clarified*, 230 Kan. 166, 630 P.2d 1129 (1981), *cert. denied*, 50 U.S.L.W. 3592 (Jan. 25, 1982). Because constitutional application of the Price Protection Act restricts price increases equally under either ERG contract clause, as ERG admits, J.S. 12 n.22, this secondary issue is mooted by a resolution of the constitutional question.

15. *Railroad Comm'n v. Rowan & Nichols Oil Co.*, 310 U.S. 573 (1940); *Railroad Comm'n v. Pacific Gas Co.*, 302 U.S. 388 (1938); *Champlin Refining Co. v. Corporation Comm'n*, 286 U.S. 210 (1932); *Cedar Rapids Gas Light Co. v. City of Cedar Rapids*, 223 U.S. 655 (1912); *Willcox v. Consolidated Gas Co.*, 212 U.S. 19 (1909).

tion that does not achieve its stated goal. To draw this picture, ERG incompletely states the legislative history of the Act and inaccurately defines its terms, which were intended to and admittedly do save Kansas natural gas consumers almost $128,000,000 in increased gas costs over five years.[16] The Act additionally produces an obvious beneficial impact on inflation and unemployment in industries that utilize that natural gas.

During a winter with significant public outcry against high natural gas prices, ERG conspicuously seeks imposition of new, unprecedented constitutional restrictions on a state's ability to control those prices that are vital to the state's economy and to the general welfare of its citizens. ERG's indirect proposals would interfere with the NGPA intrastate pricing system, which expressly embraced state imposition of these controls, and would cripple the "partnership and understanding among the federal government [and] the states" that the NGPA envisioned for energy management.[17]

I. The Price Protection Act Legitimately Addresses a Bona Fide State Goal in an Area That Kansas Has Traditionally Regulated, and the Act Does Not Represent Special Legislation

A review of the events preceding enactment of the Price Protection Act clearly reveals that the Kansas decision to limit intrastate gas price increases did not represent legislative favoritism to KPL in its litigation with gas producers. To the contrary, gas producers' early instigation of this litigation was an attempt both to evade

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16. This figure was not disputed by ERG or by any other gas producer in testimony before the State legislature. J.S.App. 73a-74a.

17. Executive Office of the President, Energy Policy and Planning, *The National Energy Plan* 89 (1977).

legitimate state controls then under legislative consideration, and to obtain maximum intrastate ceiling prices that the NGPA established expressly subject to these state controls.

A. The Producers Attempt to Obtain Contingent NGPA Benefits, Provided Subject to State Controls, While Evading State Imposition of Those Controls

This and other litigation arose after the Congressional Conference Committee reported that the new, potentially quite high NGPA intrastate price ceilings would be expressly subject to more stringent state regulation.[18] The prospect of these more stringent controls in Kansas was quite clear even before NGPA price ceilings became effective.

In November, 1978, Kansas elected a new governor who had campaigned on a promise of restraining utility price increases. On January 23, 1979, in his first address to the state legislature, Governor Carlin emphasized the need for legislative action in the field of energy, noting the "mistaken belief that unguided private enterprise will be responsive to the larger public interest."[19] On February 6, 1979, S.B. 252 was introduced in the Kansas Senate and proposed severe limitations on the operation of indefinite price escalator clauses in intrastate natural gas contracts.[20]

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18. Joint Explanatory Statement of the Comm. on Conference, H.R. Rep. No. 1752, 95th Cong., 2d Sess, 125, *reprinted in* [1978] U.S. Code Cong. & Ad. News 9041. *See also* 15 U.S.C. § 3432(a) (Supp. IV 1980).

19. Office of the Governor of the State of Kansas, *Governor's Legislative Message and Budget Report* 11 (Jan. 23, 1979).

20. Kansas Legislative Information System, *1979 Senate and House Actions Report* 45 (May 14, 1979). S.B. 252 proposed a one year absolute prohibition of any price increases under indefinite price escalator clauses in intrastate Kansas contracts. The bill thereafter limited those price increases to an annual 5-1/2% rate. *Id.*

On February 7, 1979, the Senate referred S.B. 252 to the Committee on Energy and Natural Resources, which scheduled hearings on the bill for February 21, 1979.[21]

In light of these developments, Mesa Petroleum on February 15, 1979, declared, and on February 16 filed suit to enforce, termination of three large gas supply contracts with KPL because of KPL's refusal to pay for Mesa's old gas the maximum NGPA Section 102 new gas price.[22] Mesa's notice of termination was several weeks premature under contract provisions,[23] and Mesa claimed, based upon enactment of NGPA ceiling prices, contractual price increases then forbidden by interim federal regulations.[24]

While S.B. 252 was still pending in the legislature, the less restrictive Price Protection Act was introduced as H.B. 2680 in the Kansas House.[25] After Governor Carlin urged the legislature to take positive action on the latter bill, and threatened to call the legislature into a special session on May 15, 1979, if it did not,[26] a Special Joint

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21. *Id.*

22. Mesa filed its action *solely* for a declaratory judgment that it terminated its contracts, and not for money damages or for payment of higher prices, as ERG represents to this Court. J.S. 6; *see Mesa Petroleum Co. v. The Kansas Power and Light Company*, 229 Kan. 631, 629 P.2d 190, *clarified*, 230 Kan. 166, 630 P.2d 1129 (1981), *cert. denied*, 50 U.S.L.W. 3592 (Jan. 25, 1982).

23. Mesa's contracts provided that termination could occur no earlier than 95 days after the price increase allegedly occurred on December 1, 1978, and thus was not proper until March, 1979. Cf. J.S.App. 69a.

24. "The establishment of maximum lawful prices under the NGPA shall not trigger indefinite price escalator clauses in existing intrastate contracts." 18 C.F.R. 270.205 (historical comment, Dec. 1, 1978), 43 Fed. Reg. 56448, 56463 (Dec. 1, 1978), *vacated*, FERC Order No. 23, 44 Fed. Reg. 16904 (March 20, 1979).

25. Kansas Legislative Information System, *1979 Senate and House Actions Report* 96 (May 14, 1979).

26. Office of the Governor of the State of Kansas, Press Release (May 7, 1979).

Committee conducted three days of hearings on the bill. The Committee heard favorable testimony regarding the bill's provisions from governmental agencies, including the Kansas Energy Office and the State Corporation Commission, from labor union representatives, rural electrical cooperatives, municipal utilities and larger private utilities, including KPL.[27]

The Special Committee thoroughly examined the status of natural gas production in Kansas. The Committee heard detailed descriptions of the natural gas situation in Oklahoma and the Oklahoma legislative response to the problem. The Committee examined documentary analyses of the gas markets and conditions in both states, and reviewed studies of gas production, reserves and market destination breakdowns in Kansas.[28] The Committee also considered the potential impact of NGPA ceiling prices on all gas in Kansas.[29]

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27. Kansas Legislative Research Department, *Minutes, Hearings Before the Special Comm. on Energy and Natural Resources* (June 25, 1979). *See also* Special Comm. on Energy and National Resources, *Report on 1979 H.B. 2680-Restriction of the Operation of Indefinite Price Escalator Clauses in Certain Gas Purchase Contracts* (May 14, 1979) ["Special Committee Report"] J.S.App. 71a, 79a.

28. Kansas Legislative Research Department, *Oklahoma Experience on Senate Bill No. 49*, Report to the Special Comm. on Energy and Natural Resources (June 25, 1979); R. Powers, *Production of Crude Oil and Natural Gas in Kansas*, Kansas Legislative Research Department (March 20, 1979); Kansas Energy Office and Kansas Corporation Comm'n, *Background Memorandum on H.B. 2680* (May 8, 1979). Kansas Legislative Research Department, *Overview of the Natural Gas Policy Act of 1978* 8-24 (March 1979).

29. Kansas Legislative Research Department, *The Effect of the Natural Gas Policy Act (NGPA) of 1978 on Kansas* (March 27, 1979). One administrator for two Kansas cities told of a 539% increase for natural gas delivered to those cities over a previous 4-1/2 year period, and the consequent financial difficulties those cities face. Kansas Legislative Research Department, *Minutes, Hearings Before the Special Comm. on Energy and Natural Resources, supra* note 27.

Representatives of eleven separate natural gas producers, and a representative of an association of over 1,000 independent oil and gas producers in Kansas, testified in opposition to the bill.[30] The producers presented the same arguments to the Special Committee regarding the bill's alleged deficiencies that ERG here makes to this Court. The Special Committee nevertheless reported the bill favorably to both legislative bodies.[31]

On the Senate floor, H.B. 2680 underwent several changes, including several amendments on points offered as criticisms of the Bill by the Special Committee minority.[32] The bill passed by overwhelming majorities in both legislative bodies,[33] and was signed into law by Governor Carlin. Gas producers obtained hearings on the Act in the 1980 legislative session and urged rescission of the Act based on its alleged impact on the industry.[34] The legislature also received the annual report on the impact of the Act, as prepared by the Kansas Corporation Commission pursuant to the Act.[35] After reviewing these facts, however, the legislature did not reverse its prior decision.

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30. *Id.*, at 4-7.

31. Kansas Legislative Information System, *1979 Senate and House Actions Report* 98 (May 14, 1979); Special Committee Report, *supra* note 27. J.S.App. 71a, 80a.

32. Six amendments to the Act were offered; on roll call votes four passed and two were defeated. Senate and House Journals, *Proceedings of the Legislature of the State of Kansas*, 1979 Sess. 785-88 (May 14, 1979).

33. The Senate voted in favor of passage 36-3. The House voted in favor of passage 92-31. Kansas Legislative Information System, *1979 Senate and House Actions Report* 98 (May 14, 1979). Only 7 of the 14 originally dissenting members of the Special Committee voted against the Bill. Senate and House Journals, *Proceedings of the Legislature of the State of Kansas*, 1979 Sess. 787, 973 (May 14, 1979).

34. Kansas Legislative Research Department, *Minutes, Hearings Before the Sen. Comm. on Energy and Natural Resources* (Feb. 20, 1980).

35. *See* Kan. Stat. Ann. § 55-1411 (Supp. 1980) (Commission required to monitor and to report on impact of Act on gas supplies in Kansas); J.S.App. 63a.

Nothing in this history indicates any illegitimate purpose underlying the Act. ERG made no attempt below, where this case was submitted on stipulated facts, to substantiate on the record any claim of improper legislative motive. KPL sent two corporate officers to testify before the legislature in favor of the proposed bill, which was already drafted and pending before that body.[36] This constituted remarkably less involvement with the legislative process than that of gas producers, who actively lobbied the legislature in opposition to state controls, and who sought from Congress and FERC the introduction of deregulated prices to increase their already high profits.

To support its claim of an illegitimate purpose, ERG solely relies on a single statement in the Special Committee minority report, which the full legislature rejected. The subjective feelings of fourteen minority members, seven of whom ultimately voted in favor of this legislation, cannot vitiate a legislative decision that was properly made for legitimate reasons. In constitutional challenges under the contract clause, "legislation [cannot] be set aside by courts because of the fact, if it be such, that it has been sponsored and promoted by those who advantage from it." *Cohen v. Beneficial Industrial Loan Corp.*, 337 U.S. 541, 550-51 (1949).

Moreover, ERG erroneously assumes that KPL could benefit from enactment of the Price Protection Act. KPL is a regulated utility that many earn only that return, and charge only those rates, that the State Corporation Commission allows. KPL is entitled to pass through to its consumers, whether residential or industrial, every increase in cost for the gas that it buys, either for dis-

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36. Kansas Legislative Research Department, *Minutes, Hearings Before the Special Comm. on Energy and Natural Resources* 3 (June 25, 1979). *See also* J.S.App. 79a.

tribution to consumers or to generate electricity for distribution to others. The Commission has previously noted that, because of this pass through, the Act did not benefit the utility. Kansas consumers received the benefit from this legislation. *See* R. Vol. II at 399. KPL's involvement in this litigation arose from its desire to defend, on behalf of its consumers, valuable, lower-priced gas contracts that enable it to provide a public service at a reasonable cost. This does not impugn the purpose and effect of the Kansas Act.

B. The Price Protection Act Is Consistent With Kansas' Extensive History of Natural Gas Regulation and Serves a Legitimate Goal

Despite ERG's attempt to depict the Price Protection Act as illegitimate legislative favoritism, ERG cannot dispute that the price control legislation here addresses an admittedly legitimate governmental goal. "A legislative power to create price ceilings has, in 'countries where the common law prevails,' been 'customary from time immemorial . . . .' Its exercise has regularly been approved by this court." *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 768-69 (1968), quoting *Munn v. Illinois*, 94 U.S. 113 (1876). Exercise of this power in the field of natural gas regulation, "a subject which especially comes within [a state's] lawful authority," *Ohio Oil Co. v. Indiana*, 177 U.S. 190 (1900), is even less subject to question. "The price of gas distributed through pipelines for public consumption has been . . . long and consistently recognized as a proper subject of [state] regulation."[37]

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37. *Federal Power Comm'n v. Natural Gas Pipeline Co.*, 315 U.S. 575, 582 (1942) citing *Railroad Comm'n v. Pacific Gas Co.*, 302 U.S. 388 (1938).

Nor can ERG contend, in the face of the sudden price increases anticipated under the NGPA,[38] that state exercise of this legislative power is inappropriate.[39] Similar price increases in petroleum, for example, recently caused both the United States and other western governments to impose price controls on that energy commodity.[40]

This Court has uniformly upheld reasonable state natural gas price controls against challenges that they violate the due process and contract clauses of the United States Constitution.[41] This Court has dismissed as insubstantial contract clause challenges to state statutes that prohibited a party from producing gas on his own land and compelled unitized management and production of his gas resources.[42] This Court has uniformly rejected contract

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38. *See Impact of Natural Gas Prices on Consumers: Hearings before the Subcomm. on Intergovernmental Relations of the Senate Comm. on Governmental Affairs*, 96th Cong., 1st Sess. 9, 292 et seq. (1979) (statements of C. Curtis, Chairman, FERC, and Sen. Sasser) (Estimated first year price increases under NGPA exceeded $5 billion, far in excess of OPEC oil price increases in 1975).

39. In response to the NGPA, both Oklahoma and New Mexico also enacted price control legislation restricting intrastate price increases. Oklahoma Natural Gas Price Protection Act, Okla. State. Ann. tit. 52, §§ 2601.1-13; Act of March 17, 1979, 1979 N.M. Laws, ch. 97 at 306 (amending N.M. Stat. Ann. §§ 62-7-3 to 62-7-9 (1978)).

40. *See Mapco, Inc. v. Carter*, 573 F.2d 1268 (Emer. Ct. App. 1978); Natural Gas Pricing Agreement Act, ch. 38, 1975 Alta. Stat.; Energy Act of 1976, c. 76, § 4 (England); Parsons, *Prices Justification in Australia—The First Twenty Months*, 6 Fed. L. Rev. 367, 368-70 (1975).

41. *Cities Serv. Gas Co. v. Peerless Oil & Gas Co.*, 340 U.S. 179 (1951) (Oklahoma minimum gas prices); *Cedar Rapids Gas Light Co. v. City of Cedar Rapids*, 223 U.S. 655 (1912) (city-imposed maximum gas prices); *Willcox v. Consolidated Gas Co.*, 212 U.S. 19 (1909) (New York maximum natural gas prices); *See Union Dry Goods v. Public Service Comm'n*, 248 U.S. 372 (1919) (state maximum electricity prices do not violate contract clause).

42. *Palmer Oil Corp. v. Phillips Petroleum*, 204 Okla. 543, 231 P.2d 997 (1951), *appeal dismissed sub nom. Palmer Oil Corp.*

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clause challenges to state legislative restrictions on well spacing,[43] state imposition of price controls on contracts executed prior to any regulation,[44] and state orders that prohibited sales of a producer's natural gas under contracts for various uses.[45]

The Kansas controls challenged here are completely consistent with Kansas' history of natural gas regulation, and do not represent the "sharp departure from Kansas' prior policy" that ERG claims.[46] Kansas is among the largest[47] natural gas producing states in the country, and the legislature has, since the beginning of the century, regulated virtually every aspect of intrastate natural gas production. Kan. Rev. Stat. Ann. 1923 ch. 55 at 781, 1935 ch. 55 at 1174, 1188.[48] More than three decades ago, one commentator referred to Kansas as "one of the articulate and forthright proponents of state regulatory powers" in

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Footnote continued—

v. Amerada Petroleum Corp., 343 U.S. 390 (1952); *Anderson v. Corporation Comm'n*, 327 P.2d 699 (Okla. 1957), *appeal dismissed*, 358 U.S. 642 (1959); *Hunter Co. v. McHugh*, 202 La. 97, 11 So.2d 495 (1942), *appeal dismissed*, 320 U.S. 222 (1943).

43. *Patterson v. Stanolind Oil & Gas Co.*, 182 Okla. 155, 77 P.2d 83 (1938), *appeal dismissed*, 305 U.S. 376 (1939).

44. *Fort Smith Spelter Co. v. Clear Creek Oil & Gas Co.*, 267 U.S. 231 (1925).

45. *Henderson Co. v. Thompson*, 300 U.S. 258, 266 (1937); *Bandini Petroleum Co. v. Superior Court*, 284 U.S. 8, 22 (1931).

46. J.S. 18 n.28; J.S. 17.

47. In the first half of this century, Kansas was ranked third among the states for most natural gas reserves. Hardwicke, *Some Consequences of Fears by Independent Producers of Gas of Federal Regulation*, 19 Law & Contemp. Prob. 342, 350-51 (1954).

48. Federal Oil Conservation Board, *The Oil and Gas Conservation Statutes* (1933). By 1933 Kansas was among 24 states that had statutes regulating production and consumption of natural gas. The Kansas Supreme Court has acknowledged the authority of the State Corporation Commission to fix prices at the wellhead. *Kansas-Nebraska Natural Gas Co. v. State Corp. Comm'n*, 169 Kan. 722, 222 P.2d 704 (1950).

the field of natural gas regulation. Note, 26 Notre Dame L. 561, 567 (1951). Intricate regulation of natural gas production in Kansas continues to be a part of Kansas policy.[49]

As ERG notes here, "[t]he presence or absence of previous state regulation has been identified by this Court as a factor to be considered in assessing the constitutionality of a legislative impairment of contractual rights." J.S. 17 n.27. This Kansas regulatory pattern was one factor relied upon by the federal district court that upheld this same legislation against an identical constitutional challenge.[50] The question in this litigation is whether the subject Kansas controls are reasonably related to the legitimate goal that the statute was intended to serve.

II. The Price Protection Act Is Reasonably Related to Its Legitimate Goal and Does Not Substantially Impair ERG's Contracts

The contract clause is not offended by "legislation adjusting the rights and responsibilities of contracting parties [if based] upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption." *United States Trust Co. v. New Jersey*, 431 U.S. 1, 22 (1977). Under this standard ERG here assails the Price Protection Act because it allegedly fails to regulate

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49. Kan. Stat. Ann. §§ 55-701 et seq; Kan. Admin. Regs. 82-2-100 to 82-2-800. Two bills regulating natural gas production and the extension of Corporation Commission jurisdiction over additional production were introduced in the 1981 legislative session. Kansas Legislative Information System, *1981 Senate and House Actions Report* 6 (April 9, 1981). Governor Carlin recently announced plans to introduce far more severe price controls on intrastate natural gas in response to the conditions of the recent winter. Office of the Governor of the State of Kansas, Press Release (Feb. 19, 1982).

50. *Edmiston v. State Corp. Comm'n*, No. 79-1335 (D. Kan. Nov. 24, 1980), *modified*, (D. Kan. Jan. 13, 1981), *appeal docketed*, No. 81-1197 (10th Cir. Feb. 23, 1981).

gas prices in Kansas severely enough to achieve a constitutional result. While ERG admits that Kansas "could have set maximum prices for all natural gas," J.S. 22 n.35, the Kansas Legislature allegedly erred because the enacted controls affect too few contracts and too few prices. ERG overlooks the intent and purpose of the state legislation to achieve, as does the NGPA, a compromise approach to higher natural gas prices.

A. The Provisions of the Act Further the Statutory Goal

The Price Protection Act reflects the Kansas Legislature's acknowledgment of the same policies that underlay enactment of the NGPA: gradual introduction of higher natural gas prices in a manner that "assure[s] that economic health is maintained and improved, that unemployment rates are reduced, and that inflationary pressures are minimized."[51] Under the NGPA, Kansas had the right to regulate all intrastate gas prices—in essence to substitute state pricing for NGPA Section 105 prices, and for other gas category price ceilings as applied to intrastate gas. Rather than fixing, as EGR recommends, a single maximum ceiling price that would more severely limit contract prices, Kansas adopted an intrastate pricing system that closely resembles the federal pricing system for interstate gas. Consistent with the NGPA's purpose, the Price Protection Act thus aids the equalization of interstate and intrastate market prices for natural gas.[52]

The Price Protection Act, like the NGPA, "concentrates the greatest price increases on those categories of gas where the potential for increasing supplies is the greatest." *Economic Analysis of the NGPA*, *supra* note 4, at 9. The

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51. *Economic Analysis of the NGPA*, *supra* note 4, at 2.

52. *See* id., at 8-10.

Act provides for new and stripper well gas the higher NGPA incentive prices for those gas categories to stimulate both exploration for new gas resources and continued production of marginal resources in Kansas. Kan. Stat. Ann. § 55-1406 (Supp. 1980), J.S.App. 61a-62a. The NGPA itself acknowledges that the reasons for providing these incentive prices do not apply to old gas already flowing on the date of the NGPA's enactment. *See Pennzoil, supra,* 645 F.2d at 372 & n.22.

ERG herein challenges that part of the pricing system that Kansas has imposed on old intrastate gas under contract—that part of the Price Protection Act that Kansas has substituted for Section 105 of the NGPA. The Price Protection Act provides that indefinite price escalator clauses in these contracts may operate, if their terms so provide, up to the escalating Section 109 price for various categories of old gas, a price equal to the highest NGPA price for old gas in the interstate market. Kan. Stat. Ann. § 55-1405 (Supp. 1980); J.S.App. 61a.[53]

ERG challenges this provision because it bars receipt of a Section 102 new gas price for its old intrastate gas under contract. ERG does not, however, challenge the federal imposition of the Section 109 price ceiling, or in many cases an even lower price, on old interstate gas under Sections 109 and 104, or on old intrastate gas under Section 105 or 106 for contracts with prices lower than the

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53. *See* 47 Fed. Reg. 4505 (Feb. 1, 1982). Section 109 establishes the price ceiling for old interstate gas not subject to a FERC regulatory rate on November 8, 1978. Section 109 also establishes the price ceiling for old intrastate gas not subject to contract on November 8, 1978. Section 109 additionally functions as a "catch-all" and applies to gas that does not qualify under any other NGPA category. 15 U.S.C. § 3319(a) (Supp. IV 1980). Price escalations for this gas are restricted to the same inflation factor increase permitted in Kansas by the Price Protection Act. *See* 15 U.S.C. §§ 3314(b)(1)(A), 3319(b)(1)(B), 3331(a) (Supp. IV 1980).

Section 102 price.[54] ERG neither claimed nor introduced evidence below to show that the Section 109 price allowed in Kansas for its old gas is an unreasonable price that does not permit substantial profit under its contracts.

ERG assails the Price Protection Act as ineffective and unnecessary because of various limitations in the Act. ERG's argument is inconsistent with the line of Supreme Court cases that strike down legislation imposing "a drastic impairment when an evident and more moderate course would serve its purposes equally well." *United States Trust Co. v. New Jersey*, 431 U.S. 1, 30-31 (1977).[55]

ERG agrees that the Price Protection Act would be constitutional if it severely impaired its contracts by absolutely fixing a price for all intrastate gas at a single, non-escalating level, thus keeping ERG's prices below that to which ERG is presently entitled. J.S. 22. If such severe legislation would be constitutional under these same circumstances, as ERG concedes, the lesser impairment involved here necessarily satisfies the test adopted in *Allied Structural Steel v. Spannaus*, 438 U.S. 234 (1978). "The severity of the impairment measures the height of the hurdle the state legislation must clear." *Id.* at 245.

Each limitation in the Act challenged by ERG expressly limits the reach of the statute to allow price increases consistent with the philosophy of the NGPA, while minimizing interference with producers' contracts. The Act exempts new and stripper well gas from its controls to permit for that gas the same NGPA incentive price

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54. *See, e.g., Ecee, Inc. v. FERC*, 645 F.2d 339, 356-49 (5th Cir. 1981) (party seeking Section 109 ceiling instead of lower Section 105).

55. *See Faitoute Iron & Steel Co. v. City of Asbury Park*, 316 U.S. 502 (1942); Tribe, *American Constitutional Law* 467-69 (1978); Hale, *The Supreme Court and the Contract Clause* (pt. 1), 57 Harv. L. Rev. 512, 551-57 (1944).

that the NGPA allows in the interstate market. The Act restricts only contracts executed prior to April 20, 1977, the date on which President Carter announced the impending introduction of higher natural gas prices, because contracts executed thereafter could have anticipated receipt of higher NGPA prices.

ERG's contention that the Act fails to regulate sufficient volumes of gas is also misleading. The NGPA specifically reserved to the state the power to regulate only intrastate gas prices.[56] Kansas would face obvious constitutional problems if it attempted to regulate interstate gas prices.[57]

Of the intrastate gas subject to state control, the Price Protection Act addresses that gas which is subject to indefinite price escalator clauses—40% of all Kansas' intrastate gas.[58] Only that gas has the potential for sudden, substantial price increases in conjunction with new NGPA interim price ceilings.[59] Restriction of indefinite escalator clauses also constitutes a less severe impairment than regulation of fixed price escalator clauses. The former only disrupts parties' anticipation of some *unspecified* price increase, while the latter denies parties a definite

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56. *See* Joint Explanatory Statement of the Comm. on Conference, H.R. Rep. No. 1752, 95th Cong., 2d Sess. 124, *reprinted in* [1978] U.S. Code Cong. & Ad. News 9041.

57. *See, e.g., Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n,* 332 U.S. 507 (1947); *Illinois Natural Gas Co. v. Central Ill. Pub. Serv. Co.,* 314 U.S. 498 (1941); *Public Utils. Comm'n v. Attleboro Steam & Elec. Co.,* 273 U.S. 83 (1927).

58. *See* Special Committee Report, J.S.App. 73a.

59. The contracts herein are illustrative. Aside from indefinite price escalator clauses, these contracts provide only for fixed price escalations at rates of $.02 every two years. J.S.App. 66a. From October 1, 1979, to October 1, 1981, the NGPA Section 102 price claimed by ERG increased from $2.292 to $2.909, for an increase of $.617, more than 30 times the fixed price increases contemplated in the contracts. *See* 47 Fed. Reg. 4505 (Feb. 1, 1982).

price increase on a specific date for which they had specifically bargained.

Legislative action to restrain indefinite price escalator clauses is hardly unique. This Court has upheld federal regulatory orders that limited or prohibited price increases under these clauses in interstate contracts.[60] Effective January 1, 1985, the NGPA itself imposes and continues indefinitely restrictions on all price increases under indefinite price escalator clauses for all intrastate gas. 15 U.S.C. § 3315(b)(3) (Supp. IV 1980).[61]

The NGPA also contains numerous specific prohibitions on the operation of indefinite price escalator clauses.[62]

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60. *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 781-84 (1968); *Federal Power Comm'n v. Texaco, Inc.*, 377 U.S. 33 (1964). *See also* Comment, *The FPC and Indefinite Price Escalation Clauses: Remedy for an Administrative Breakdown*, 73 Yale L.J. 1283, 1290-93 (1964).

61. Section 105(b)(3) provides that indefinite price escalator clauses in intrastate contracts may not operate to allow price increases in excess of the monthly inflation escalator, plus a small growth factor. This is virtually the same percentage price escalation allowed for Section 109 old gas, which the Price Protection Act allows until deregulation in 1985. *See* 15 U.S.C. § 3319(b) (Supp. IV 1980). This NGPA limitation on intrastate gas price escalator clauses first appeared in an amendment to the House and Senate Conferees' Agreement in Principle, which outlined the compromise between the two legislative bodies' disparate positions on deregulation. The amendment provided that *"state authority to limit or prohibit the operation of any indefinite price escalator clause or limit their effect . . . would not be preempted."* Congress chose not to enact interim restrictions on intrastate price escalator clauses in recognition that individual states might *"prescribe more stringent limitations on the operation of such clauses."* Staff of House Comm. on Interstate and Foreign Commerce and Senate Comm. on Energy and Natural Resources, 95th Cong., 2d Sess., *Natural Gas Pricing Agreement Adopted by the Conferees on H.R. 5289* 18-19 (1978).

62. FERC Order No. 23, 44 Fed. Reg. 16899-900 (March 20, 1979). *See generally* 18 C.F.R. § 154.93 (1979); S. Rep. No. 1126, 95th Cong., 2d Sess. 83 (1978). *See also* 95 Cong. Rec. S. 15021 (daily ed. Sept. 13, 1978) (statement of Senator Jackson).

(Continued on following page)

The maximum NGPA price ceilings for each gas category also provide a basic ceiling restriction on the operation of any escalator clause for gas in that category, as the court noted in *Edmiston*. Even deregulation legislation presently pending in the U.S. House of Representatives contains an absolute prohibition on the operation of any indefinite price escalator clause in a deregulated marketplace. H.R. 4885, 97th Cong., 1st Sess. (1981).

Consistent with past and present Federal law, the Price Protection Act is reasonably related to its purpose of price control and the gradual introduction of the higher natural gas prices ultimately expected. Like the federal controls, the state controls do not seriously interfere with ERG's ability to profit under these contracts.

B. The Act Does Not Substantially Impair ERG's Contracts

As the lower federal court noted in *Edmiston*, the Price Protection Act did not frustrate any reliance interest of gas producers in their indefinite price escalator clauses. This is not a case where ERG has contracted for the sale of its gas at a specific price and the state has thereafter ordered a lower price for the sale of that gas. ERG's only "contractual right" at issue here is its "right" to raise its old gas price to the NGPA Section 102 new gas incentive price, an absolute ceiling provided by Section 105 in the absence of more stringent state controls.

Footnote continued—

Additionally, NGPA Section 313 specifically provides that no price paid for purchases of high-cost gas under NGPA Section 107(c), or for emergency purposes under Section 302, may be taken into account in applying an indefinite price escalator clause in intrastate or interstate contracts. 15 U.S.C. § 3373 (Supp. IV 1980).

By definition, ERG had no reliance interest in any NGPA Section 105 ceiling level, either before or after NGPA enactment. ERG at most proposes a reliance interest in the "operation" of its escalator clause to insure *some* higher price—a price governmentally allowed for its gas. ERG, however, does receive that increased price allowed by federal and state governments.[63] ERG is simply unwilling to accept that old gas ceiling for its old intrastate gas. ERG seeks the benefits of the NGPA without accepting its limitations.

ERG suggests that the Price Protection Act is unnecessarily broad because it overlooks less restrictive alternatives. ERG suggests that it should be permitted to terminate its contracts and sell its gas elsewhere, or that the State Corporation Commission should disallow the pass through of increased gas costs to consumers. Allowing ERG to sell its gas elsewhere, however, constitutes a serious loss to Kansas consumers of the natural gas they desire to purchase, and compels consumers either to go

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63. ERG's contracts specifically provide for only those price increases that future state regulation would allow. Both indefinite price escalator clauses are expressly made subject to "all relevant present and future state and federal laws." J.S.App. 69a. The contracts further provide that "neither party shall be held in default for failure to perform hereunder if such failure is due to compliance with such laws." J.S.App. 70a.

ERG contends that, because its termination *procedure* was not expressly "subject to state law," it retained the "right to terminate the contracts if it could not receive the . . . enumerated price increases." J.S. 15 n.25. These enumerated price increases, however, are those provided in the escalator clauses, which *are* expressly subject to future state laws. J.S.App. 66a-70a.

KPL promised in this contract to pay price increases subject to state law, and ERG retained the right to terminate its contracts if KPL refused to pay those price increases permitted by state law. Nothing in the contract provides, as ERG represents, a right to terminate the contracts if state law prohibits a price increase and KPL refuses to pay the unlawful price. Both courts so interpreted the contracts below, and ERG should be bound by that ruling here. *Graver Mfg. Co. v. Linde Co.*, 336 U.S. 271, 275 (1949).

without gas or to purchase it from other producers at even higher prices.

Nor can the State Corporation Commission, by denying KPL a pass through of these costs, make gas price increases disappear. In the absence of a pass through, KPL's expenses would seriously rise and require other rate increases. KPL's earnings are already regulated by the Corporation Commission. The state can and does control through that body the level of earnings at which KPL operates. ERG here challenges the additional regulation that the state decided was necessary to control utility prices more effectively.

ERG claims that the Price Protection Act severely denies it the "market value" that it "reasonably expected" under its contracts. J.S. 15, 24. The NGPA, however, was enacted on the premise that classical economics and theories of "free market prices" do not apply to the American natural gas market.[64] Additionally, the Section 102 incentive price sought here is intended to reflect the Btu equivalent price for petroleum,[65] a "market price" that only results from cooperative pricing agreements of petroleum exporting countries beyond the reach of American antitrust laws.[66] Provision of this price as an incentive to encourage new production may serve a legitimate purpose. Denial of this incentive price, determined by an oligopoly that otherwise does not control the American natural gas

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64. *Economic Analysis of the NGPA, supra* note 4, at 5.

65. *See* H.R. Rep. No. 496, 95th Cong., 1st Sess. (pt. 4) 96 (1977), *reprinted in* [1978] U.S. Code Cong. & Ad. News 8549; H.R. Rep. No. 543, 95th Cong., 1st Sess. 44, *reprinted in* [1978] U.S. Code Cong. & Ad. News 7711-12; J. Carter, 1 Pub. Papers 681 (1977).

66. *International Ass'n of Machinists & Aerospace Workers v. OPEC*, 477 F.Supp. 553 (C.D.Cal. 1979), *aff'd*, 649 F.2d 1354 (9th Cir. 1981).

market, does not seriously impair ERG's contract rights regarding old gas for which production incentives are unnecessary.

ERG twice presented to the legislature its arguments regarding the purported economic effects of the Act and whether it benefits the consumers in Kansas. As stated in *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 477-78 (1934), however, "whether the legislation is wise or unwise as a matter of policy is a question with which we are not concerned." Price control legislation applicable to existing contracts need only appear reasonable and related to a proper legislative purpose to pass constitutional inquiry. The Price Protection Act satisfies this standard.

III. The Kansas Decision Properly Resolves the State Law Question That ERG's Government Pricing Clause Did Not Provide a Price Increase on December 1, 1978, and This Decision Does Not Conflict With the NGPA, With Decisions of the Federal Courts or FERC, or with Congressional Intent

ERG's second Question Presented is identical to that for which this Court recently denied certiorari in *Mesa Petroleum*. It alleges that the Court below misconstrued NGPA Section 105(b) and thereby "immutably fixed the November 9 price as the Section 105(b)(1) [ceiling] price" J.S. 27. The inherent contradiction in ERG's position reflects that the Court did not so hold.

NGPA Section 105 is the ceiling price for ERG's contracts, regardless of the escalation provision relied upon. If the decision below holds that the Section 105 price ceiling freezes the contract price, then no price escalation is possible under any provision in these contracts, including

the price redetermination clause. ERG states, however, that "the Kansas Supreme Court's ruling on Section 105 (b) (1) of the NGPA affects only the government pricing provisions of the contracts, not the wholly independent price redetermination provision." J.S. 12 n.22. ERG thus admits that the holding does not interpret Section 105 to bar the claimed price increase, but relies instead on the specific terms of the government pricing clause to deny the price increase.

The only question actually presented on this record is whether one particular clause in ERG's contracts provides a price increase on a designated date. The NGPA does not grant any seller any right to increased gas prices, but establishes maximum price ceilings available only if the contract has a sufficient escalation mechanism to authorize collection of the higher price. The Court below addressed, as it did in *Mesa Petroleum*, whether ERG's government pricing clause is contractually sufficient to trigger, based upon NGPA enactment, an escalation of the contract price to NGPA price ceilings. J.S.App. 15a.

ERG's contract clause provides for a price increase when a government authority "fixes a higher price" for natural gas that ERG's contracts can adopt. ERG claims its price increase based upon Congressional enactment of an intrastate price ceiling equal to the *lower* of the NGPA Section 102 price and the "price under the terms" of the contract. ERG claims that this governmental action "fixes a *higher* price" within the terms of its contracts sufficient to trigger a higher contract price.

Enactment of the NGPA allegedly "fixes a higher price," however, only because the "price under the terms" of ERG's contracts allegedly equals the higher Section 102

price. The price so equals the 102 price only if the clause has already escalated. The circularity of the argument within the terms of ERG's government pricing clause is obvious.

Regardless of whether the parties intended Congressional action to trigger higher prices, as the Court below found, J.S.App. 12a, the Court ultimately held that, under ERG's government pricing clause, Congress did not adequately "fix a higher price." Enactment of the NGPA "did not trigger a price increase *because the contracts herein did not contain a sufficient escalation mechanism.*" J.S.App. 15a. The decision below is conclusive on this question of state law.[67]

KPL respectfully submits that the second question raised in ERG's appeal is simply not available on this record, nor is it one properly for review in this Court.

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67. Both the Federal Energy Regulatory Commission and the Fifth Circuit Court of Appeals hold that state law controls whether an intrastate contract produces a price increase under specific circumstances. Both state that the identical language in two separate contracts could produce different price escalations, or no price escalations whatsoever, based upon the application of differing state law. *See Pennzoil Co. v. FERC*, 645 F.2d 360, 386 (5th Cir. 1981), *cert. denied*, 50 U.S.L.W. 3547 (Jan. 11, 1982); *The Kansas Power and Light Company v. Mesa Petroleum Co.*, Docket No. GP79-4 (FERC Aug. 10, 1979).

CONCLUSION

For the foregoing reasons, appellee respectfully submits that this appeal fails to raise a substantial federal question and should accordingly be dismissed.

Respectfully submitted,

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Appellant's Reply Brief

No. 81-1370

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

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APPELLANT'S REPLY TO MOTION TO DISMISS

1. KPL has portrayed itself as a relatively passive bystander in a controversy purportedly between natural gas producers and utility consumers. KPL contends (at 14) that even if the escalator clauses at issue were given effect, it would be "entitled" to have the Kansas Corporation Commission ("KCC") pass the resulting cost increases through to KPL's customers. Thus, the argument continues, the Kansas Price Protection Act's abrogation of these escalator clauses would not benefit KPL, and so the state statute cannot be deemed the kind of legislative favoritism proscribed by the Contract Clause.

This contention is belied by the plain terms of the contracts at issue and the law governing public utilities. Each contract expressly and correctly acknowledges that the KCC may disapprove the "pass-on" of an increased cost for natural gas. App. 69a.[1] Indeed, litigation has been before this Court involving an instance of the KCC's refusal to allow a Kansas utility to pass through a certain portion of its natural gas costs to its consumers. See *State Corporation Commission of Kansas v. Wichita Gas Co.*, 290 U.S. 561 (1934).[2] It is therefore understandable that KPL, which is the largest purchaser of intrastate gas in Kansas, became the legislation's "main proponent", App. 81a, because it feared that without help from the legislature its profits would suffer considerably.[3] See J.S. 22.

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[1] In case of disapproval, KPL admits (at 25 n.63) that it would have to agree to pay the increased price or risk ERG's exercise of its option to terminate the contract on 30 days' written notice.

[2] KPL itself must have doubted whether the KCC would approve a pass-through here, especially in view of the fact that by April 25, 1979 (when the Kansas statute was first introduced), the KCC had not yet acted on the application for a pass-through that KPL had filed on December 7, 1978. It hardly appeared that approval of the pass-through would be routine or assured.

[3] KPL grossly understates (at 14) the degree of its involvement in the passage of H.B. 2680. It was a widely and openly recognized

2. Assuming that increases in the price of natural gas would be borne by consumers, KPL argues (at 9) that the Kansas statute imposes price controls that "are vital to the states' economy and to the general welfare of its citizens." Thus, according to KPL (at 8, 16), ERG's challenge to the Kansas statute does not present a substantial federal question because this Court has in the past sustained various instances of state price regulation. But the cases cited by KPL are inapposite and do not decide this case. All but two of the cases do not involve the Contract Clause; rather, they concern whether the price of natural gas is a proper subject of state regulation and whether the general regulatory controls there at issue satisfied the requirements of due process.[4]

In *Union Dry Goods Co.* v. *Georgia Public Service Corp.*, 248 U.S. 372 (1919), and *Fort Smith Spelter Co.*

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fact in Kansas that KPL was the most ardent advocate of the bill. See Wichita Eagle, May 3, 1979, at 1, col. 1, 2A, col. 1 (KPL, "the state's largest buyer of Kansas natural gas, lobbied hard to bring the bill up for consideration"); Topeka Sunday Capital-Journal, May 6, 1979, at 16, col. 1 (KPL was the "industry leader in the battle"); Wichita Eagle, May 11, 1979, at 1B, col. 1, 3B, col. 6 ("KPL is among the most vocal proponents of the measure."); The Kansas City Star, May 15, 1979, at 6, col. 1.

According to one of the legislative reports cited by KPL (at 12 n.28), of the four major field purchasers of natural gas in Kansas, "the largest by far in terms of gas volumes involved is the Kansas Power & Light Company. KPL has an estimated 22 billion cubic feet per year supplied pursuant to contracts with indefinite price escalator clauses, compared to a statewide total of approximately 50 billion cubic feet per year." Kansas Energy Office and Kansas Corporation Commission, *Background Memorandum on H.B. 2680*, at 6 (May 8, 1979). If required to pay the escalated price under its contracts, KPL stood to bear over half of the increase borne by all four major field purchasers combined. *Id.*

[4] *E.g.*, *Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*, 340 U.S. 179, 186 (1950); *Cedar Rapids Gas Light Co.* v. *City of Cedar Rapids*, 223 U.S. 655 (1912); *Willcox* v. *Consolidated Gas Co.*, 212 U.S. 19 (1909). See also *FPC* v. *Natural Gas Pipeline Co.*, 315 U.S. 575, 582 (1942) (due process clause of the Fifth Amendment).

v. *Clear Creek Oil & Gas Co.*, 267 U.S. 231 (1925), which do involve the Contract Clause, the authority sustained was that of a public service commission to establish universally applicable rates charged by a public utility. This is an entirely different situation from the one involved here. The Kansas Price Protection Act does not impose or purport to impose price controls of general applicability. The statute restricts the operation of indefinite (but not fixed) escalator clauses in contracts executed before April 20, 1977 (but not thereafter),[5] affects only a small portion of the Kansas natural gas sold in the intrastate market,[6] and—most important—allows a purchaser like KPL to agree to waive whatever limited restrictions the statute imposes. See generally J.S. 7-8, 18-19; App. 81a. By giving private parties permission to "voluntar[ily] renegotiat[e] . . . price provisions contained in [their] contracts," Section 8 of the Price Pro-

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[5] KPL suggests (at 22) that the statute invalidates only indefinite escalator clauses executed prior to April 20, 1977, because on that date President Carter submitted to Congress his National Energy Plan, and thus "contracts executed thereafter could have anticipated receipt of higher NGPA prices." KPL provides no support from the legislative history for this rationalization. Moreover, we perceive no neutral principle that dictates (a) sanctions for natural gas producers that foresaw, prior to April 20, 1977, the possibility that the value of their gas would be increased by federal action, but (b) rewards for producers that foresaw, after that date, that such favorable action might be forthcoming.

[6] We have acknowledged (J.S. 18-20) that had the Kansas legislature enacted price controls that served "a broad societal interest," the legislation might have survived this Court's Contract Clause analysis. KPL responds (at 18-19, 21) that if more general legislation would be acceptable, then the "lesser impairment involved here" *a fortiori* must satisfy the Constitution. This argument misperceives the interests protected by the Contract Clause. As we have shown (J.S. 20), it is the "extremely narrow focus" of state legislation abridging contract rights that is damning. The Kansas statute was not "one enacted to protect a broad societal interest [but] rather . . . a narrow class," *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234, 248-49 (1978), and it therefore cannot survive constitutional scrutiny.

tection Act, K.S.A. § 55-1408, potentially nullifies the statute's purported protection of consumers. See J.S. 22-23. We are unaware of any other kind of price control legislation that allows private parties to agree to disregard the controls.[7]

Thus, this Court's precedents—concerning conventional applications of the Contract Clause, which ERG does not challenge—do not render insubstantial ERG's challenge to this legislation.[8] Indeed, this Court already has intimated that it would find legislation like this Kansas statute in violation of the Contract Clause.[9]

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[7] To be sure, the Oklahoma statute from which the Kansas statute was copied contains the identical provision for voluntary renegotiation of prices. Constitutional challenges to the Oklahoma statute currently are pending. See J.S. 25 n.37.

The New Mexico statute cited by KPL (at 16 n.39) set, for a two-year period, a price ceiling for *all* natural gas contracts, which could not be exceeded by virtue of any price escalation, redetermination or renegotiation. Moreover, New Mexico regulated the price of natural gas even before enactment of the NGPA.

[8] In order to conclude that the federal constitutional question presented is not a substantial one, this Court must determine that the question presented "is wholly formal, is so absolutely devoid of merit as to be frivolous, or has been so explicitly foreclosed by a decision or decisions of this court as to leave no room for real controversy . . . ." *Equitable Life Assurance Society* v. *Brown*, 187 U.S. 308, 311 (1902); see Stern & Gressman, *Supreme Court Practice* § 4.28, at 319 (5th ed. 1978). Such is not the case here.

[9] In *Arkansas Natural Gas Co.* v. *Arkansas R.R. Comm'n*, 261 U.S. 379 (1923), where the commission responsible for regulating utilities and fixing rates refused, pursuant to a statutory prohibition, to fix flat rates higher than those in existing contracts between a natural gas company and its public utility purchasers, this Court observed:

> "While a State may exercise its legislative power to regulate public utilities and fix rates, notwithstanding the effect may be to modify or abrogate private contracts . . . there is, quite clearly, no principle which imposes an obligation to do so merely to relieve a contracting party from the burdens of an improvident undertaking. The power to fix rates, when exerted, is for the public welfare, to which private contracts must yield; but

3. We have acknowledged, J.S. 17-18 n.28, that § 602 of the NGPA affords the States the authority to establish generally applicable maximum lawful prices lower than those prescribed in the NGPA. KPL relies heavily upon this provision (at 1, 2, 5, 9, 10) to justify the Kansas legislature's restriction of indefinite escalator clauses. Even leaving aside the question whether the Kansas statute imposes "price controls" within the meaning of § 602, see J.S. 17-18 n.28, it is quite clear that § 602 is not an invitation for States to pass laws violative of the United States Constitution. If the state legislation lacks the characteristics described by this Court in *Home Building & Loan Association* v. *Blaisdell*, 290 U.S. 398 (1934), and its recent progeny, it is unconstitutional; and Congress could not have intended otherwise.[10]

4. KPL paints a picture (at 10-14) of carefully considered legislation not enacted to appease the state's largest public utility. But KPL retouches the picture

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it is not an independent legislative function to vary or set aside such contracts, however unwise and unprofitable they may be. *Indeed the exertion of legislative power solely to that end is precluded by the contract impairment clause of the Constitution.*" *Id.* at 382-83 (emphasis added) (citations omitted).

[10] KPL cites (at 5) one sentence of the Conference Committee Report concerning a State's authority, under § 602, to impose limitations on the operation of indefinite escalator clauses. But in so stating, the Conference Committee contemplated that such limitations would be part of and ancillary to a State's imposition of constitutional, generally applicable price controls. This would be consistent both with the rationale underlying the NGPA's establishment of the § 102 price as a ceiling on the operation of indefinite escalator clauses, and with this Court's decision in *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 782 (1968). There, this Court upheld an order of the Federal Power Commission that set maximum area rates for natural gas and prohibited "price increases that exceed the area maximum rates, if the increases are the products of certain varieties of contractual price escalation clauses." The Court explained that "to permit producers to breach the area maximum rates by implementation of such clauses would not be 'in accordance with the principles upon which a rate structure should be based.'"

to suit its position, and puts an unduly favorable gloss on the legislature's consideration of H.B. 2680. Several of the facts stated by KPL as evidence of the legislature's "serious and lengthy deliberations" are immaterial or misleading. For example, KPL suggests (at 13 & n.32) that the problems addressed in the minority report were cured by amendments on the floor of the Senate. The fact is that some of the adopted amendments were merely technical, and *all* of them concerned facets of the Kansas statute not involved in this case. Senate and House Journals, *Proceedings of the Legislature of the State of Kansas*, 1979 Sess. 785-88 (May 14, 1979). Even after adoption of the amendments, the basic thrust of the bill was unchanged.[11]

5. KPL attempts (at 5-6 & n.13, 23-24 & nn.60-62) to prejudice consideration of the question presented by characterizing indefinite escalator clauses as against the public interest and generally undesirable. But Kansas has never before prohibited or restricted the use of these clauses;[12] KPL, a large and sophisticated public utility,

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[11] Another example of KPL's misleading presentation involves S.B. 252. That bill was introduced in February of the 1979 legislative session, received little consideration by the legislature and indeed never got past the Senate committee to which it was referred. Another involves KPL's drawing of certain inferences favorable to H.B. 2680 from the fact that some members of the committee minority ultimately voted for passage. But this does not detract from the merits of the objections to the bill stated in the minority report. Indeed, one of those who switched to an affirmative vote (after passage was assured) recorded that he did so "reluctantly," because the bill would provide at best "short-term savings for a small segment of [Kansas] citizens" while leading to adverse long-term results. *Proceedings of the Legislature, supra*, at 790 (remarks of Senator Morris). Others expressed the same views. *Id.* 789-91.

[12] While KPL claims (at 17) that Kansas historically has regulated "virtually every aspect of intrastate natural gas production," it is undisputed that Kansas has *never* before regulated the *price* charged by natural gas producers. See, *e.g.*, App. 80a. Thus, contrary to KPL's assertions, the Kansas statute's abrogation of certain indefinite escalator clauses is not "consistent with Kansas' history

freely agreed to the inclusion of such clauses in a third of its contracts;[13] and the NGPA specifically contemplates that indefinite escalator clauses will be allowed to operate up to the § 102 ceiling. See J.S. 27 & n.39.[14]

6. KPL criticizes ERG (at 2) for "seek[ing] for [its] old intrastate gas the maximum NGPA new gas incen-

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of natural gas regulation, and . . . represent[s] the 'sharp departure from Kansas' prior policy' that ERG claims."

[13] As KPL's Executive Vice President cogently observed in testimony before the Kansas legislature in February 1979: "Producers and ourselves have never been under any type of wellhead price control. Negotiations for the price of gas have always been between a willing buyer and a willing seller with no government intervention." Testimony of J.G. Williamson before the Senate Comm. on Energy and Natural Resources, at 1 (Feb. 28, 1979).

[14] KPL relies (at 23) upon certain limitations imposed by the FPC on indefinite escalator clauses pursuant to a regulatory format which predated the NGPA. We have already shown (see n.10, *supra*), that the FPC limitation involved in the *Permian Basin* cases proscribed the operation of indefinite escalator clauses only to the extent they exceeded general area-wide rates then set by that agency. This is the same type of prohibition found within the NGPA itself. In sustaining the constitutionality of the regulation in *Permian Basin*, the Court relied in part on the fact that parties affected by the regulation could abandon their activities rather than comply with the prohibition. 390 U.S. at 770, 772. That option is not afforded under the Kansas statute. See J.S. 21 & n.34. Before *Permian Basin*, the FPC had proscribed the use of certain escalator clauses, but that proscription was *prospective* only, and did not abrogate existing contracts as is the case here. See *FPC* v. *Texaco, Inc.*, 377 U.S. 33 (1964). *FPC* v. *Texaco* did not involve a constitutinoal challenge. Moreover, the constitutionality of any federal limitation depends on the due process clause of the Fifth Amendment and not the Contract Clause, which does not apply to the federal government. Hale, *The Supreme Court and the Contract Clause: III*, 57 Harv. L. Rev. 852, 890 (1944).

KPL also refers (at 24) to a purported "absolute prohibition" in a single natural gas deregulation bill (H.R. 4885, 97th Cong., 1st Sess. (1981)) among many now pending, which was introduced by one Congressman, and has not been considered by the relevant House committee. In any event, the bill does not contain an "absolute prohibition," but rather allows indefinite escalator clauses to operate, as in the NGPA, up to a statutory ceiling.

tive prices." KPL seems to argue (at 2, 6, 19-21 & n.53) that ERG suffered no impairment of contract because the Kansas statute's *qualified* allowance of prices up to the ceiling set by § 109 of the NGPA [15] is consistent with the plan envisioned by the NGPA itself.[16]

In so arguing, KPL seeks to create the false impression that the NGPA distinguishes bluntly between the general categories of "old" and "new" gas, treating "old" gas as deserving of a lower price such as Kansas has prescribed for the gas here at issue. In fact, the NGPA draws finer and more carefully considered distinctions. In its pricing mechanisms for "old" gas, for example, the federal statute distinguishes, *inter alia*, between certain categories of old intrastate gas (not under contract as of the date of enactment), as to which the lower ceiling of § 109 applies, and, on the other hand, old intrastate gas (like that involved here) which was under contract as of the date of enactment and is subject to contractual provisions for price escalation. As to the latter category, Congress was aware that in November 1978

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[15] Section 109, 15 U.S.C. § 3319, establishes price ceilings for natural gas not within the specific categories covered by other sections of Title I of the NGPA, including, *inter alia*, "old" intrastate gas that was not subject to an existing contract as of the NGPA's enactment date. The § 109 maximum price is substantially lower than the § 102 maximum price. See 18 C.F.R. §§ 271.202, 271.902, 271.101(a) (Table 1) (1981) (excerpted in the Appendix hereto). Indeed, as we have shown (J.S. 23 n.36), until April 1980 the § 109 maximum price was lower than the contract price under these contracts, even without any increases based on the indefinite escalator clauses.

[16] The § 109 allowance is qualified in that the Kansas statute by its terms prohibited *any* escalation of the contract price, even up to the § 109 price, from December 1, 1978 until March 1, 1979. And, as we previously have noted (J.S. 23 n.36), KPL has taken the position that ERG at best could have the contract price for the gas here at issue redetermined to the § 109 price as of November 1981, but could not thereafter take advantage of the monthly escalation provided for in § 109 until the next opportunity for price redetermination in November 1983. See generally J.S. 23 n.36.

intrastate gas under existing contracts often carried a price higher than the § 109 ceiling, and it accordingly prescribed for such gas more favorable treatment under § 105(b)(1), which incorporates the substantially higher new gas price schedule of § 102. See n.15, *supra*. KPL concedes (at 5) that the gas here at issue is governed by § 105. KPL's implication that ERG cannot complain of the Kansas statute's substitution of less than even the full § 109 price for the § 102 price, to which it is entitled under its contracts and the NGPA, is therefore quite misleading. And it is the Kansas statute's selective substitution of an unjustifiably low price for the price to which ERG is entitled that forms the basis of ERG's constitutional claim.

7. Contrary to KPL's contention (at 27-29), the question whether ERG is entitled to the § 102 price for its gas under the government pricing clause is not an issue of state law. Two questions pertaining to that clause were presented below: (1) whether the parties thereby intended to trigger the escalation of prices up to those authorized by the NGPA; and (2) if they so intended, whether § 105(b)(1) of the NGPA authorizes payment to ERG of the § 102 price. The first question concerns contract interpretation and is an issue of state law; the latter, however, requires interpretation of a federal statute.

The Kansas Supreme Court held that "the parties *intended* that the government price escalation clauses be triggered by enactments such as the NGPA." App. 14a (emphasis in original). The court then was compelled to construe the federal statute, and it held, based on its erroneous reading of the statutory language "price under the terms of the existing contract," that § 105(b)(1) of the NGPA precluded escalation to the § 102 price. See J.S. 26-27. Thus, construction of the federal statute was critical to the Kansas Supreme Court's result, and its ruling on this issue conflicts squarely with interpretations given § 105(b)(1) by FERC and the Fifth Circuit. See J.S. 28-29 & nn. 41 & 42. Indeed, both FERC and the

United States already have strongly urged this Court to correct the erroneous interpretation of the NGPA by the Kansas Supreme Court.[17]

CONCLUSION

This Court should note probable jurisdiction and set this case for plenary review.

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March 16, 1982

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[17] They did so by way of a brief *amicus curiae* urging summary reversal in *Mesa Petroleum Co.* v. *The Kansas Power & Light Co.*, 229 Kan. 631, 629 P.2d 190, *clarified*, 230 Kan. 166, 630 P.2d 1129 (1981), *cert. denied*, 50 U.S.L.W. 3592 (U.S. Jan. 25, 1982), a case upon which the Kansas Supreme Court expressly relied to reach the result below. Justices Brennan, Marshall and Blackmun noted that they would have granted certiorari in the *Mesa Petroleum* case. ERG respectfully requests that the Court reconsider whether it should correct the error of the Kansas Supreme Court in the context of a case in which a substantial federal constitutional question also is presented. The constitutional issue was not presented in *Mesa Petroleum*.

APPENDIX

Excerpt from Table I—Natural Gas Ceiling Prices
(18 C.F.R. § 271.101(a) (1981))

Month	§ 102	§ 109
December 1978	$2.078	$1.630
January 1979	2.096	1.639
February 1979	2.116	1.650
March 1979	2.136	1.661
April 1979	2.156	1.672
May 1979	2.177	1.684
June 1979	2.198	1.696
July 1979	2.220	1.708
August 1979	2.244	1.722
September 1979	2.268	1.736
October 1979	2.292	1.750
November 1979	2.314	1.762
December 1979	2.336	1.774
January 1980	2.358	1.786
February 1980	2.381	1.799
March 1980	2.404	1.812
April 1980	2.428	1.825
May 1980	2.453	1.839
June 1980	2.478	1.853
July 1980	2.504	1.867
August 1980	2.532	1.883
September 1980	2.560	1.899
October 1980	2.588	1.915
November 1980	2.614	1.929
December 1980	2.640	1.943
January 1981	2.667	1.957
February 1981	2.698	1.975
March 1981	2.729	1.993
April 1981	2.761	2.011

Amicus Brief

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No. 81-1370

IN THE
Supreme Court of the United States
OCTOBER TERM, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,
v.
THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF OF AMICUS CURIAE STATE CORPORATION COMMISSION OF THE STATE OF KANSAS IN SUPPORT OF APPELLEE'S MOTION TO DISMISS

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ENERGY RESERVES GROUP, INC.,
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Appellee.

On Appeal from the Supreme Court of Kansas

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

Comes now the State Corporation Commission of the State of Kansas (State Commission) and moves the Court for leave to file the attached brief *amicus curiae* in this case, pursuant to Supreme Court Rule 36.4. As this brief is being filed on behalf of the State Commission by the General Counsel, as Special Attorney General for the State of Kansas pursuant to Supreme Court Rule 36.4, consent of the attorneys for appellant and appellee is not required.

The interest of the *amicus* State Commission in this case stems from its character as an independent regulatory body responsible for the regulation of oil and gas utilities within the State of Kansas. As such, the *amicus* State Commission is responsible for making gas well

category determinations under the Natural Gas Policy Act of 1978 (NGPA) (15 USC § 3301 *et seq.*), and for the implementation and enforcement of the provisions of the Kansas Natural Gas Price Protection Act (K.S.A. 55-1401 *et seq.* (1980 Supp.)). Because of these dual statutory responsibilities, the *amicus* State Commission has a substantial interest in assuring that the constitutionality of the Price Protection Act is sustained, and that the NGPA and the Price Protection Act are interpreted in a consistent fashion.

The brief of *amicus* State Commission approaches the question of the constitutionality of the Price Protection Act from the perspective of a state agency with regulatory responsibilities under both the NGPA and the Price Protection Act. This approach should present the Court with additional insight to assist it in disposing of the pending appeal.

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On Appeal from the Supreme Court of Kansas

BRIEF OF AMICUS CURIAE STATE CORPORATION COMMISSION OF THE STATE OF KANSAS IN SUPPORT OF APPELLEE'S MOTION TO DISMISS

INTEREST OF AMICUS CURIAE

The salient facts of this case are concisely stated in the Statement of the Case contained in appellee's Motion to Dismiss. For purposes of brevity, *amicus* State Corporation Commission of the State of Kansas (State Commission) adopts appellee's Statement of the Case and Questions Presented.

Title I of the Natural Gas Policy Act of 1978 (NGPA) (15 U.S.C. § 3301, *et seq.*) established an intricate set of controls for the wellhead price of natural gas, including natural gas produced and marketed intrastate under existing contracts. (15 U.S.C. § 3315) The NGPA also authorized the gas producing states to institute such price control legislation for intrastate gas as they might

deem necessary and appropriate because of the passage of the NGPA. (15 U.S.C. § 3431(c)(2)(a).) Pursuant to this Congressional directive, the Kansas Legislature enacted the Kansas Natural Gas Price Protection Act (Price Protection Act) (K.S.A. § 55-1401 (1980 Supp.)), which established a ceiling price for natural gas produced and consumed within Kansas.

Amicus State Commission is a state administrative agency vested with broad regulatory authority over electric and gas utilities doing business in Kansas. This authority includes responsibility for making gas well category determinations pursuant to the NGPA (15 U.S.C. § 3413), and the implementation and enforcement of the provisions of the Price Protection Act (K.S.A. § 55-1409 (1980 Supp.)). As a consequence, the Commission has a substantial interest in assuring that the constitutionality of the Price Protection Act continues to be sustained, and that the NGPA and the Price Protection Act are interpreted in a consistent fashion.

REASONS FOR DISMISSING APPEAL

I. The Opinion Of The Kansas Supreme Court Is In Accord With The Decisions of This Court And Presents No Substantial Question.

The instant proceeding was commenced as, and has remained throughout, a contract termination case. Energy Reserves Group, Inc. (ERG), sought judicial approval of its attempt to terminate its intrastate gas supply contract with The Kansas Power and Light Company (KP&L). Initially, ERG argued that the mere passage of the NGPA triggered the indefinite price escalation clause contained in the contract, thereby vesting ERG with the contractual right to collect the NGPA § 102 new gas price for the old intrastate gas sold under the contract. At a later date ERG added a second theory, arguing that the periodic price redetermination clause contained in the contract obligated KP&L to escalate the contract price up to the NGPA § 102 new gas price level

upon redetermination. According to ERG, when KP&L declined to pay these escalated prices, ERG had the right to terminate the contract.[1]

In its decision disposing of these two issues, the Kansas Supreme Court held that the contractual language contained in the indefinite price escalation clause was insufficient to warrant the collection of the NGPA § 102 price, which Congress intended to be paid for newly discovered gas. This determination was in conformity with the Congressional intent in passing the NGPA,[2] the FERC regulations implementing that statute,[3] and judicial decisions[4] which have interpreted it. Since the language of the indefinite escalation clause was insufficient to justify the claimed price escalation, the attempted termination of the contract was ineffectual.

It was the attempted termination under price redetermination clause which implicated the Price Protection Act, and thereby presented ERG with the opportunity to allege a constitutional violation. In dealing with this issue, the Kansas Supreme Court concluded that this redetermination clause would have authorized the escalation of the contract price up to the NGPA § 102 new gas price, but that its operation was moderated by the Price Protection Act. According to the Kansas Supreme Court, this statute limited the price escalation available to ERG under this contract to the NGPA § 109 price. In responding to ERG's constitutional attack on the Price Protection Act, the Kansas Supreme Court carefully applied the criteria established by this Court to the statute, and found it a valid exercise of the state's police power which was reasonable and necessary under the circumstances.

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[1] J.S. at 8-9.

[2] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978).

[3] 44 F.R. 16895, CCH Vol. II § 30,040 (March 13, 1979).

[4] *Pennzoil Co. v. Federal Energy Regulatory Commission*, 645 F.2d 360, 374-75 (1981).

A review of the salient provisions of the Price Protection Act demonstrates that it is a carefully drafted statute designed to deal with the gas price upheaval brought about by the NGPA, but in a fashion which fits into the regulatory scheme established by the NGPA. The Price Protection Act moderates the operation of indefinite price escalation clauses contained in intrastate gas supply contracts by limiting the price which can be collected under them to the lower NGPA § 109 price, rather than the NGPA § 102 price which Congress intended as an incentive price for newly discovered gas. This statute does not deprive gas producers of all benefits under the NGPA, nor does it immutably freeze the price to be paid for intrastate gas. What the Price Protection Act does do is prohibit gas producers from collecting new gas prices for old intrastate gas, and limit them to a more slowly escalating NGPA ceiling price. This limitation on the operation of indefinite price escalation clauses in intrastate contracts terminates on the same date as the gradual deregulation provisions contained in the NGPA.

In reaching its conclusion as to the constitutionality of the Price Protection Act, the Kansas Supreme Court carefully reviewed and correctly applied the pertinent decisions of this Court concerning the proper interpretation of the Contract Clause. Because of the utter routineness of this decision and its patent correctness concerning the alleged constitutional issue, no substantial question has been posited sufficient to necessitate review by this Court. An examination of the decision rendered by the Kansas Supreme Court reinforces this conclusion.

A. *The Price Protection Act Imposes Only A Modest And Transitory Burden On Affected Contracts.*

This Court has long recognized that the Contract Clause does not impose an absolute barrier to state legislative efforts to redress social and economic imbalances by the exercise of their police powers but has instead

developed a flexible standard for such cases. Since it is axiomatic that when the legislature acts in this economic area it will be disturbing existing contracts, this Court has indicated that a modest burdening of an existing contract will not be sufficient to invalidate a statute under the contract clause. This Court has said:

> . . . [T]he first inquiry must be whether the state law has, in fact, operated as a substantial impairment of a contractual relationship. The severity of the impairment measures the height of the hurdle the state legislation must clear. Minimal alteration of contractual obligations may end the inquiry at the first stage.[5]

The Price Protection Act does not, contrary to the assertions of ERG, render invalid the central term of its contract with KP&L. Rather, this statute moderates the operation of the redetermination clause in a reasonable fashion. Instead of allowing ERG to collect the higher NGPA § 102 price, intended for new gas and set artificially high to encourage *new* production, it allows them to collect the NGPA § 109 ceiling price. Under the Price Protection Act, gas producers such as ERG are receiving and will continue to receive the NGPA § 109 price as it escalates upwards.

Two other facts strongly indicate that the impairment imposed on ERG by the Price Protection Act is minimal. First, the escalation clauses contained in the contract are specifically made subject to "all relevant present and future state and Federal laws."[6] Since ERG voluntarily made the terms of the contract, including both price escalation clauses, subject to future state laws such as the Price Protection Act, it should not be heard to complain that its contractual relationship is burdened

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[5] *Allied Structural Steel v. Spannaus*, 438 U.S. 234, 244-45, 57 L.Ed. 2d 727 (1978).

[6] J.S. at 69a.

by the passage of just such a statute to which the contract is made subject. One federal district court has already held the presence of such a clause vitiates any claim of an impairment sufficient to sustain a Contract Clause violation.[7]

Second, the very statute upon which ERG relies specifically authorized the type of intrastate gas price control legislation passed by the Kansas Legislature. Congress foresaw that the passage of the NGPA would cause a quantum leap in intrastate gas prices, far exceeding the expectations of the parties, due to the operation of indefinite price escalation clauses. Knowing that this would disastrously disrupt the economics of gas producing states such as Kansas, Congress specifically gave these states authorization in the NGPA to deal with the problems. § 3431(c)(2)(a) of the NGPA states:

> Nothing in this Act shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such state which does not exceed the applicable maximum lawful price, if any, under Title I of this Act.

The intent of this provision was explained by the Joint Explanatory Statement of the Committee on Conference, where it said:

> The conference agreement provides that nothing in this Act shall affect the authority of any state to establish or enforce any maximum lawful price for the sales of gas in intrastate commerce which does not exceed the applicable maximum lawful price, if any, under Title I of this Act. *This authority extends to the operation of any indefinite price escalator clause.* (Emphasis supplied.)[8]

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[7] *Edmiston v. State Corporation Commission*, No. 79-1335 (D. Kan. Nov. 24, 1980), *modified* (D. Kan. Jan. 13, 1981), *appeal docketed* No. 71-1197 (10th Cir. Feb. 23, 1981).

[8] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 124-25 (1978).

In passing the Price Protection Act, the Kansas Legislature was exercising its police power to reapportion the economic dislocation caused by the passage of the NGPA, just as Congress authorized in § 3431(c)(2)(a) of the NGPA. ERG should not be heard to complain that its right to a higher contract price under the NGPA has been infringed by the Price Protection Act, when the very statute upon which ERG relies authorizes just such a limitation. The insubstantial nature of the burden imposed upon ERG's contractual expectations should, in accordance with this Court's holding in *Allied Structural Steel v. Spannaus*, *supra*, bring this inquiry to an end. As this Court stated in *El Paso v. Simmons*:

> This Court's decisions have never given a law which imposes unforeseen advantages or burdens on a contracting party constitutional immunity against change. (Citations omitted.) Laws which restrict a party to those gains reasonably to be expected from the contract are not subject to attack under the Contract Clause, notwithstanding that they technically alter an obligation of a contract.[9]

B. *The Price Protection Act Accomplishes An Important Social Goal.*

In passing the Price Protection Act, the Kansas Legislature was seeking to achieve three interrelated goals. It was attempting to moderate the disruptive impact the passage of the NGPA would have upon the Kansas intrastate gas market, and on the Kansas economy as a whole. It was trying to fairly apportion between suppliers and consumers the burdens and benefits of the gradual gas price escalation mandated by the NGPA. And it was attempting to give the Kansas gas users some modicum of protection from rapid and unintended escalation of intrastate gas prices.

In a major gas producing state such as Kansas, many industrial concerns are dependent upon intrastate gas for

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[9] 397 U.S. 497, 515, 13 L.Ed. 2d 466 (1965).

their energy. Any abrupt price change has a ripple affect throughout the state's economy which can result in severe dislocation. As a consequence, the effect of the passage of the NGPA on intrastate gas prices was of vital concern to the Kansas Legislature, as it was to her sister state of Oklahoma. This concern led both of these gas producing states to address these broad societal concerns by passing legislation to moderate the impact of the NGPA on intrastate gas prices.

ERG argues that the absence of a declared emergency is a fatal constitutional flaw in the Price Protection Act.[10] This position is ill founded. As this Court indicated in *Allied Structural Steel v. Spannaus*, a declared emergency is no longer considered a constitutional prerequisite. As the Court stated:

> This is not to suggest that only an emergency of great magnitude can constitutionally justify a state law impairing the obligations of contracts. (Citations omitted.)[11]

ERG also argues that in passing the Price Protection Act, the Kansas Legislature was attempting to avert the very consequences of deregulation which Congress had deemed to be in the public interest.[12] It is difficult to understand how the Kansas Legislature could be subverting the objectives of the NGPA by exercising the authority which that very statute granted the Legislature in the precise manner envisioned by the Congress. Again quoting from the Joint Statement of the Committee on Conference:

> The conference agreement also cedes the Federal Government's authority to further limit the operation of indefinite price escalator clauses to State governments

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[10] J.S. at 17.

[11] 438 U.S. 234, 249 at footnote 24, 57 L.Ed. 2d 727 (1978).

[12] J.S. at 17.

> wishing to do so. The Congress, by adoption of this section, recognizes the right of States to prescribe more stringent limitations on the operation of such clauses than those prescribed herein.[13]

ERG denigrates the Price Protection Act by asserting that it does not go far enough, because it fails to control the prices charged by Cities Service, an interstate pipeline company which supplies 71% of the residential and commercial gas consumed in Kansas.[14] This is a curious argument. Apparently, ERG feels that the Price Protection Act is unconstitutional because it fails to restrict the price of interstate gas, over which the Kansas Legislature has no jurisdiction. By failing to exercise jurisdiction which it does not have, the Kansas Legislature has, according to ERG, fallen into constitutional error.

C. *The Price Protection Act Is A Reasonable And Necessary Act Which Serves An Important Public Purpose.*

The Kansas Legislature unequivocally stated its opinion that the Price Protection Act was both reasonable and necessary to protect Kansas from the economic disruption which would have resulted due to the uncontrolled escalation of intrastate gas prices caused by the passage of the NGPA. As the Special Committee on Energy and Natural Resources stated:

> The NGPA of 1978 marked a radical reversal of the federal policy toward the pricing of natural gas. This new policy is directed toward increasing the price of gas, with the ultimate goal of deregulation of gas pricing . . . .
>
> However, as a result of this legislation, many producers of natural gas, especially those whose contracts contain indefinite price escalation clauses, will

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[13] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978).

[14] J.S. at 18.

> reap unanticipated, windfall financial benefits. These benefits bear no real relationship to the costs of production of new gas, and are even more remotely related to old gas production costs. They accrue solely because of the reversal of federal policy.
>
> It is clear that the burden of the increased gas costs will be passed on by the utility companies directly to the consumer. The producers will benefit beyond any expectations they might have had only a few years ago and the consumers already buffeted by rapidly increasing inflation, including spiraling utility costs, will pay.
>
> House Bill 2680 represents a modest effort by the State of Kansas to delay somewhat the full impact on consumers of inevitable natural gas price increases of some intrastate gas from the present time through 1984. For a period of nearly six years, this bill would provide a modicum of restraint on some utility price increases.[15]

This Court has consistently maintained the position that the judiciary should defer to legislative determinations of necessity and reasonableness. As stated by the Court:

> Once we are in this domain of the reserve power of a State we must respect the 'wide discretion on the part of the legislature in determining what is and what is not necessary'.[16]

This policy of judicial deference is based upon sound policy considerations. The legislative branch is uniquely suited to weigh and balance the conflicting economic interests which clash in the area of economic legislation, while the judiciary is ill suited for this task. This prudent policy of judicial deference has kept the courts

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[15] J.S. App. at 74a-75a.

[16] *East New York Sav. Bank v. Hahn*, 326 U.S. 320, 323, 90 L.Ed. 34 (1935).

from becoming trapped in this quagmire of competing special interests.

ERG would have this Court abandon this long standing rule of deference which the Kansas Supreme Court adhered to in its decision. ERG would have the Court consider whether the minority or the majority committee report was more persuasive, determine whether the Legislature elected the right alternative course of action, and determine whether the stated goal was correctly achieved.[17] ERG would have the Court undertake all of these tasks based upon a misinterpretation of this Court's decision in *United States Trust v. New Jersey*.[18] According to ERG, this case warrants a judicial redetermination of the reasonableness and necessity of any statute whenever a party can conjure up a Contract Clause claim.

The *United States Trust* decision does not stand for such a proposition, but rather for two entirely different propositions. First, when a court reviews economic regulation, such as the Price Protection Act, it should defer to the legislative determination of reasonableness and necessity. As the Court stated:

> As is customary in reviewing economic and social regulation, however, courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure.[19]

And second, this deference by the Court is not appropriate if, *but only if*, the state's own self-interest is at stake. As the Court stated:

> As with laws impairing the obligations of private contracts, impairment may be constitutional if it is reasonable and necessary to serve an important public

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[17] J.S. at 20-21.

[18] *United States Trust Company v. New Jersey*, 431 U.S. 1, 52 L.Ed. 2d 92 (1977).

[19] *Id.*, 431 U.S. at 22-23.

> purpose. In applying this standard, however, complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State's self-interest is at stake.[20]

In this case, the Kansas Supreme Court deferred to the legislative determination of necessity and reasonableness of the Price Protection Act because the state's self-interest was not at stake. This approach was consistent with the holding in the *United States Trust* case. This Court should resist the temptation to abandon this well established rule, and to voyage into the uncharted seas, where it would sit in judgment of the legislative wisdom of choosing among various alternative courses of action each time a Contract Clause claim is presented.

ERG's attack on the reasonableness of the Price Protection Act is also misguided. ERG argues that the act suffers from a constitutional impediment because it allows the parties to renegotiate their contracts.[21] Under the ERG's analysis, this statute would have been better had it totally stripped the parties of their ability to alter in any way their contract. According to ERG, the Price Protection Act was not sufficiently draconian to be constitutional.

This argument is another attempt to convert this Court into an alternative legislative forum at which dissatisfied special interest groups can attempt to refight legislative battles under the guise of contract clause litigation. The Kansas Supreme Court resisted the temptation to become a super legislature by adhering to this Court's previous decisions. This Court should follow the same path.

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[20] *Id.*, 431 U.S. at 26.

[21] J.S. at 23.

II. The Kansas Supreme Court Properly Determined That The Contractual Language Does Not Authorize Price Escalation.

It has been recognized by Congress,[22] the FERC[23] and the Fifth Circuit Court of Appeals[24] that the escalation of the price of gas under existing intrastate gas contracts is controlled by the express terms of the contract. In analyzing the language contained in the ERG contract to determine whether price escalation was authorized, the Kansas Supreme Court went through a two-step analysis. First, it reviewed the operation of the NGPA, and specifically § 105(b)(1). Relying upon the Fifth Circuit interpretation of that section contained in *Pennzoil Co. v. Federal Energy Regulatory Commission*, the court determined that if the price under the contract on November 9th was less than the NGPA § 102 price, the price could escalate up to the NGPA § 102 price so long as the contract contains a sufficient escalation mechanism.[25]

Next, turning to the language of the contract itself, the Kansas Supreme Court concluded:

> We hold that under the terms of the government price escalator clause in these contracts, and under the applicable section of the NGPA, the November 9th gas price (which was lower than the Section 102 price) did not escalate. . . . The NGPA did not trigger a price increase because the contracts herein did not contain a sufficient escalation mechanism.[26]

Under the Kansas Supreme Court's analysis, the mere establishment of ceiling prices due to the passage of the NGPA did not trigger the escalation clause as claimed

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[22] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978).

[23] 44 F.R. 16895, CCH Vol. II § 30,040 (March 13, 1979).

[24] *Pennzoil Co. v. Federal Energy Regulatory Commission*, 645 F.2d 360, 374-75 (1981).

[25] J.S. App. at 14a.

[26] J.S. App. at 15a.

by ERG. It concluded that under the facts and circumstances of this case, the words of the contractual escalation clause did not authorize the collection of the higher price claimed by ERG. As a consequence, the attempted termination of the contract by ERG was ineffectual.

This analysis of § 105(b)(1) of the NGPA, and its application to the escalation clause contained in this contract, conforms with the intent of Congress in passing the NGPA. As stated in the Joint Explanatory Statement:

> Some intrastate contracts currently in existence contain indefinite price escalator clauses which can be triggered by a number of factors, including adjustments by the Commission of 'just and reasonable' rates established under the Natural Gas Act. *The conferees do not intend that the mere establishment of the ceiling prices under this Act shall trigger indefinite price escalator clauses in existing intrastate contracts.* (Emphasis supplied).[27]

Fundamentally, this case involves the interpretation of the meaning and operation of specific contractual terms contained in an intrastate gas supply contract. The Kansas Supreme Court interpreted that contract as not authorizing price escalation, and did so in conformity with the meaning and intent of § 105(b)(1) of the NGPA. This decision rests upon independent and adequate nonfederal grounds. Therefore, appeal of this portion of the state court judgment should not lie.

CONCLUSION

ERG seeks review of a state court opinion which decided a contractual dispute. In this decision, the Kansas Supreme Court determined that the indefinite price escalation clause had not been triggered by the mere passage of the NGPA, that the price of gas sold under the contract had not escalated, and that the attempted termination of the contract was ineffective. These conclusions

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[27] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978).

were based upon the facts and circumstances of the case, and the interpretation of the meaning and operation of the indefinite price escalation clause contained in the contract.

Additionally, the Kansas Supreme Court concluded that the operation of the Price Protection Act precluded ERG from collecting the NGPA § 102 new gas price for old intrastate gas sold under its contract based upon the operation of the price redetermination clause contained in the contract. The Kansas Supreme Court also determined, after a careful review of this Court's decisions, that the Price Protection Act was a reasonable and necessary exercise of the state's unquestioned authority to regulate intrastate gas prices, enacted in conformity with the Congressional mandate contained in the NGPA. The Kansas Supreme Court resisted the temptation to substitute its judgment for that of the legislature in the area of economic price regulation.

ERG has failed to present any substantial federal question which would warrant review of this decision. For these reasons, the Appellee's Motion To Dismiss this appeal should be granted.

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No. 81-1370

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1370

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER & LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

APPELLANT'S OPPOSITION TO MOTION OF THE KANSAS CORPORATION COMMISSION TO FILE BRIEF AS AMICUS CURIAE AND SUPPLEMENTAI MEMORANDUM IN RESPONSE TO SRETO

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APPELLANT'S OPPOSITION TO MOTION OF THE KANSAS CORPORATION COMMISSION TO FILE BRIEF AS AMICUS CURIAE AND SUPPLEMENTAL MEMORANDUM IN RESPONSE THERETO

I. OPPOSITION TO MOTION

On March 12, 1982, the Kansas Corporation Commission ("the Commission") filed with this Court a motion for leave to file a brief as *amicus curiae* supporting the motion of appellee KPL to dismiss this appeal. As is customary, the brief itself was attached to the motion. That motion and brief were filed one week out of time under Supreme Court Rule 36.1. Appellee KPL had received an extension of time until March 5, 1982, to file its motion to dismiss, and it did so on that date. Rule 36.1 required that any motion for leave to file an *amicus* brief be filed on or before that same date.

The Commission's motion for leave to file its *amicus* brief neither acknowledges that it was one week late nor contains any justification whatsoever for waiving the requirement of Rule 36.1.[1] Such disregard of this Court's Rules demands that the motion be denied.[2]

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[1] The Commission had timely notice of the jurisdictional statement since appellant had served that document upon the Kansas Attorney General on January 21, 1982. See 28 U.S.C. § 2403(b) (1976).

[2] The Commission also never asked appellant to consent to the filing of its *amicus* brief, Sup. Ct. R. 36.2, and thus appellant had no advance notice that the *amicus* brief was to be filed even on an untimely basis. The Commission contends (at 1) that consent was not required because its brief "is being filed on behalf of the State Commission by the General Counsel, as Special Attorney General for the State of Kansas pursuant to Supreme Court Rule 36.4." We have serious doubts whether the Commission is a "State" for purposes of Rule 36.4, and we question whether a brief signed by the Commission's general counsel as "Special Assistant Attorney General" constitutes sponsorship by the Kansas Attorney General as required by Rule 36.4.

The Commission's failure to comply with Rule 36.1 prejudices appellant and unnecessarily burdens this Court. The Commission motion and brief were served by first-class mail and were not received by appellant's counsel until March 16, 1982, at which time appellant had completed the printing of its reply to the motion to dismiss, for filing that same day. Such replies must be filed substantially before this Court's conferences in order to receive consideration along with the principal papers, so the reply could not prudently be delayed further. Appellant's counsel has been informed by the Clerk's Office that, as is customary, the Commission motion and brief were distributed to this Court shortly after they were filed. Accordingly, appellant must go to the additional expense of filing a supplemental memorandum to respond to the Commission's *amicus* brief, in case the motion for leave to file is granted or in case the Commission's brief is considered notwithstanding denial of the motion. See R. Stern & E. Gressman, *Supreme Court Practice* § 6.38 at 497 (5th ed. 1978).

The motion for leave to file an *amicus* brief should be denied and the brief given no weight. To allow for the chance that the motion is not denied, or that the Court will have read and considered it regardless, we feel obligated to address briefly the matters raised in the Commission brief.[3]

II. RESPONSE TO AMICUS BRIEF

1. The Commission contends (at 13-14) that ERG's constitutional analysis is faulty because we neglected to refer to the sentence in *United States Trust Co.* v. *New Jersey*, 431 U.S. 1, 26 (1977), stating that "complete deference to a legislative assessment of reasonableness and necessity is not appropriate [when] the State's self-interest is at stake." 431 U.S. at 26. The Commission argues (at 14) that since Kansas's self-interest was *not*

[3] The late *amicus* brief was "not available at the time of [appellant's] last filing," within the meaning of Supreme Court Rule 16.6.

at stake here, the Kansas Supreme Court properly gave "complete deference" to the Kansas legislature's assessment of the reasonableness and necessity of the Price Protection Act. This hypertechnical reading of *United States Trust* is belied by this Court's later Contract Clause decision in *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234 (1978), where "there was no similar element of state self-interest, but the Court indicated that the customary deference would not stand when the legislation appeared to aid 'a narrow class' and there was no showing on the record that it was necessary to advance important public goals." Note, *The Supreme Court, 1977 Term*, 92 Harv. L. Rev. 57, 95 (1978) (footnotes omitted). Indeed, neither the Commission in its brief nor the Kansas Supreme Court below acknowledged the following relevant passages within *Allied Structural Steel*:

> "Despite the customary deference courts give to state laws directed to social and economic problems, '[l]egislation adjusting the rights and responsibilities of contracting parties must be upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption.'
>
> * * * *
>
> ". . . [T]here is no showing in the record before us that this severe disruption of contractual expectations was necessary to meet an important general social problem. *The presumption favoring 'legislative judgment as to the necessity and reasonableness of a particular measure,' United States Trust Co.*, 431 U.S. at 23, *simply cannot stand in this case.*" 438 U.S. at 244, 247 (emphasis added).

The Commission's reliance on *United States Trust* is therefore wholly misplaced.[4]

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[4] Contrary to the Commission's assertion (at 10), we never claimed "that the absence of a declared emergency is a fatal constitutional flaw" in the Kansas statute. We merely noted (J.S. 22) that *Allied Structural Steel* continues to require, as an element of

2. The Commission contends (at 6) that the impairment of ERG's contracts by the Kansas Price Protection Act amounts to only "a modest and transitory burden." Even if the burden were, in fact, only "modest and transitory," which we dispute emphatically, we fail to see why it had to be borne by ERG, rather than KPL, whose contractual obligations were relieved by the Kansas statute. In this regard, the Commission does not dispute our showing (J.S. 22) that the limited public benefits to be derived from the statute could have been achieved as easily by refusing to allow KPL to "pass-on" natural gas price increases to its customers; nor does the Commission support KPL's contention (at 14) that the utility was "entitled" to have the Commission "pass-on" these price increases. See ERG Reply at 1-2.

Moreover, the Commission implicitly acknowledges the severity of ERG's impairment when it concedes (at 5) that the Kansas Supreme Court found that, absent the Price Protection Act, ERG's "redetermination clause would have authorized the escalation of the contract price up to the NGPA § 102 new gas price." On November 9, 1978, the date of the NGPA's enactment, the contract price was $1.77 per Mcf, while the § 102 price was $2.06. J.S. 8-9. Three years later, when the § 102 price was $2.94, KPL was only paying ERG $1.83 for the gas at issue. 47 Fed. Reg. 4505 (February 1, 1982). If, as the Kansas Court and the Commission acknowledge, ERG is contractually entitled to the § 102 price, the Price Protection Act's denial of that price for a six-year period can hardly be considered either "modest or transitory."

The Commission also erroneously contends (at 7) that ERG should be consoled by the fact that "[u]nder the Price Protection Act, gas producers such as ERG are receiving

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Contract Clause analysis, that courts consider whether an emergency justified the legislation at issue, 438 U.S. at 422; we also showed that the Kansas Supreme Court's finding that the Kansas statute was a response to an "emergency situation" (App. 22a) was supported neither by the record nor the statute's legislative history.

and will continue to receive the NGPA § 109 price as it escalates upward." As we have shown in our reply (at 7-9), by virtue of § 105(b)(1) of the NGPA, Congress expressly intended that the § 102 price, rather than the § 109 price, be applied to the gas here at issue. Even the Commission states (at 15) that under § 105(b)(1), "the price could escalate up to the NGPA § 102 price so long as the contract contains a sufficient escalation mechanism," and, as we have shown (see p. 4, *supra*), the Commission has also acknowledged (at 5) that the court below found that these contracts included an escalation provision triggering the § 102 price. In any event, as we have shown elsewhere (J.S. 23, n.36), ERG has received far less than the escalating § 109 price.

3. The Commission describes (at 4) the Price Protection Act as "establish[ing] a ceiling price for natural gas produced and consumed within Kansas," and alleges (at 8) that it was designed to prevent "a quantum leap in intrastate gas prices," which, in turn, would have "a ripple effect in the state's economy . . . result[ing] in severe dislocation."

We already have shown, however, that the statute's highly selective coverage excludes large portions even of Kansas *intrastate* sales and that, even if it applied to *all* intrastate sales, only a small fraction of the gas consumed in Kansas would be affected. J.S. 7-8; 18-20. Indeed, the Price Protection Act's purported goal of preventing "severe dislocations" is belied not only by the admissions of its legislative proponents (App. 75a) and by the Commission (at 9) that it would provide at best "a modicum of protection," but also by the statute's provision authorizing contracting parties to circumvent the statute's limited protections through voluntary renegotiation of prices. See J.S. 23.[5]

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[5] Contrary to the Commission's assertions (at 11), we do not attack the legislation because it "fails to control the prices charged by Cities Service, an interstate pipeline company which supplies 71% of the residential and commercial gas consumed in Kansas." We cited the Cities Service statistics, as well as the limited and

4. The Commission, as does KPL, places heavy reliance (at 8-9) upon a passage in the NGPA Conference Report noting that a State may impose limitations upon indefinite escalator clauses to assure that any lower maximum lawful prices established by that State under § 602 of the NGPA are not exceeded. The Federal Energy Regulatory Commission has made it clear that, in so providing, the conferees only "ceded to states under section 602 the authority to further limit the operation of price escalator clauses *as an adjunct* to their authority to prescribe lower maximum lawful prices for the first sale of natural gas produced within the state." 44 Fed. Reg. 16898 (March 20, 1979) (emphasis added). Under the Kansas statute, however, the selective abrogation of price escalator clauses is not "an *adjunct* to . . . lower maximum lawful prices"; it is the sole regulatory mechanism included therein. And, as we have shown (Reply 5), even if the Kansas statute is not invalid under § 602, the constitutional inquiry is not at an end, since Congress could not have intended § 602 to authorize violations of the Contract Clause.

5. The Commission also argues (at 7-8) that the scope of ERG's contractual entitlement is limited to whatever state law says it is, because the contracts contain a standard provision acknowledging that they are subject to "all relevant present and future state and federal laws." This would be the case even without any explicit acknowledgment; and it is obvious that the contracts are subject only to state or federal laws that are *valid*. ERG claims that this state law is not.

In any event, the Commission misinterprets this contract provision: ERG retained the right to terminate the contracts if it could not receive its bargained-for consideration because of a change in applicable law. This is the reason for the deliberate exemption of the termi-

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selective *intrastate* reach of the Kansas statute, to show that the legislation addresses no "important general social problem," but that it instead "clearly has an extremely narrow focus." *Allied Structural Steel*, 438 U.S. at 247-48.

nation clause of the contracts from the clause concerning applicable laws. See App. 69a-79a; J.S. 4-5.

6. Finally, the Commission contends (at 15-16), as has KPL, that the Kansas Supreme Court resolved as a matter of state law the question whether ERG was entitled to the § 102 price for its gas under the government pricing clause. The Commission's argument essentially rests on a single paragraph within the lower court's decision, which the Commission quotes in its brief without indicating that it has omitted the paragraph's first sentence.[6]

As a careful parsing of that paragraph reveals and as we have shown in detail (J.S. 25-29), a necessary predicate of the Kansas Supreme Court's ruling on this issue is its holding that the § 105(b)(1) term "price under the *terms* of the existing contract, to which such natural gas was subject on November 9, 1978" means "the *contract price* on November 9, 1978" without reference to the government pricing escalator clause. This holding is plainly a federal question.

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[6] The full relevant portion of the paragraph relied upon by the Commission provides:

> "Section 105(b)(1) of the NGPA fixes the maximum lawful price of intrastate gas as the lower of the Section 102 price or 'the price under the terms of the existing contract, to which such natural gas was subject on November 9, 1978, as such contract was in effect on such date. . . .' We hold that under the terms of the government price escalator clause in these contracts, *and under the applicable section of the NGPA*, the November 9th gas price (which was lower than the Section 102 price) did not escalate. . . ." App. 14a-15a (emphasis added).

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OCTOBER TERM, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,
v.
THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

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QUESTIONS PRESENTED

1. Whether the Kansas Natural Gas Price Protection Act, Kan. Stat. Ann. § 55-1401 *et seq.* (Supp. 1980), violates the Contract Clause of the United States Constitution when that statute relieves a utility of its contractual obligation to pay price increases mandated by long-term natural gas purchase contracts, does not further an important general social purpose, and is neither a necessary nor reasonable means of dealing with any limited public interest that the Kansas legislature may have intended to address.

2. Whether § 105(b)(1) of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3315(b)(1), precludes the operation of contractually established price escalation clauses in intrastate natural gas contracts and freezes prices to those in effect on the date of enactment of the Natural Gas Policy Act.

PARTIES BELOW

The only parties to this proceeding in the court below are those indicated by the caption of this brief. Appellant Energy Reserves Group, Inc., has no parent corporation, subsidiaries (except wholly-owned subsidiaries), or affiliates.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1370

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

BRIEF FOR APPELLANT

Appellant Energy Reserves Group, Inc. ("ERG") appeals from a final judgment of the Supreme Court of Kansas.

OPINIONS BELOW

The opinion of the Kansas Supreme Court (J.S. App. 1a-24a)[1] is reported at 230 Kan. 176, 630 P.2d 1142 (1981). The opinions of the trial court on cross-motions for summary judgment (J.S. App. 25a-41a) and on ERG's motion to reconsider (J.S. App. 42a-44a) are unreported. The journal entry of the trial court (J.S. App. 45a-49a) is unreported.

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[1] "J.S. App." refers to the appendix accompanying the Jurisdictional Statement which was filed in this appeal on January 21, 1982. "App." refers to the appendix filed with this brief. The latter appendix contains only the relevant docket entries below and an order of the Kansas Corporation Commission. Sup. Ct. Rule 30.1.

JURISDICTION

The judgment of the Supreme Court of Kansas was entered on July 17, 1981, and rehearing was denied on September 23, 1981. J.S. App. 50a. Appellant filed a timely notice of appeal in the Kansas Supreme Court on December 8, 1981. J.S. App. 51a-54a. Upon timely application, Justice White granted appellant an extension of time until January 21, 1982, to docket an appeal. J.S. App. 55a. This appeal was docketed on the latter date, and on March 29, 1982, this Court noted probable jurisdiction. See 28 U.S.C. § 1257(2) (1976).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The following constitutional provisions and statutes involved in this appeal are set forth in the appendix accompanying the Jurisdictional Statement: the Contract Clause of Article I, Section 10, of the United States Constitution (J.S. App. 56a); the relevant parts of §§ 102 and 105 of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3312 & 3315 (Supp. IV 1980) (J.S. App. 56a-58a); and the Kansas Natural Gas Price Protection Act, Kan. Stat. Ann. §§ 55-1401 through 55-1415 (Supp. 1980) (J.S. App. 58a-65a).

STATEMENT OF THE CASE

This appeal concerns a decision of the Kansas Supreme Court upholding § 4 of the Kansas Natural Gas Price Protection Act ("Kansas Price Protection Act"), Kan. Stat. Ann. ("K.S.A.") § 55-1404, which restricts the operation of certain critical price adjustment provisions in long-term intrastate natural gas purchase contracts. The Kansas Supreme Court affirmed a trial court's rejection of appellant's claim that the Kansas statute abridges Article I, Section 10, of the United States Constitution in that the legislation impairs the obligation of contracts by permitting the statute's principal sponsor, The Kansas Power & Light Co. ("KPL"), to avoid price increases

otherwise lawfully mandated by that utility's contracts for the purchase of natural gas.

Also involved in this appeal is the Kansas Supreme Court's holding that § 105(b)(1) of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3315(b)(1) (Supp. IV 1980), does not allow a price increase under one of the escalator clauses in the contracts at issue. Both the Federal Energy Regulatory Commission ("FERC") and the United States already have urged this Court to correct the Kansas court's serious misinterpretation of this key pricing provision in a major federal regulatory statute.[2]

A. The Contracts.

ERG is a natural gas producer. In September 1975, KPL entered into two long-term gas purchase contracts with ERG, both involving intrastate sales of natural gas.[3] J.S. App. 3a. Together, these contracts commit to KPL all of ERG's natural gas production from the Spivey-Grabs field in Kansas for the entire life of the field or of the associated processing plants. *Id.* ERG accepted an initial price for its gas that was lower than that offered it by other prospective purchasers in 1975, in return for KPL's agreement that the pricing schedule in each con-

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[2] They did so by way of a brief *amicus curiae* urging summary reversal in *Mesa Petroleum Co.* v. *The Kansas Power & Light Co.*, 229 Kan. 631, 629 P.2d 190, *clarified*, 230 Kan. 166, 630 P.2d 1129 (1981), *cert. denied*, 50 U.S.L.W. 3592 (U.S. Jan. 25, 1982) (No. 81-711), a case upon which the Kansas Supreme Court expressly relied to reach its result on the § 105(b)(1) issue below. Justices Brennan, Marshall, and Blackmun noted that they would have granted *certiorari* in *Mesa*. 50 U.S.L.W. 3592. The *Mesa* case, however, did not raise the constitutional question presented on this appeal.

[3] One of the contracts governs the sale of gas produced directly from the wells; the other governs the sale of remaining gas after certain recovery and processing steps are completed. J.S. App. 3a. The relevant provisions of the contracts are set forth at J.S. App. 66a-70a.

tract would include identical provisions for upward price adjustment over the term of the contract.[4]

Accordingly, each contract contains, *inter alia*, two "indefinite price escalator clauses."[5] The first is a "government pricing" clause. J.S. App. 66a. It provides for the automatic escalation of the contract price to the highest level authorized by any governmental or regulatory authority for any vintage of gas produced in Kansas. The second indefinite escalator clause is a "price redetermination" clause. J.S. App. 67a. It provides that upon request by ERG no more than once every two years the parties must agree to a new price equal to the average of the three highest prices paid for natural gas in Kansas under contracts meeting certain specifications. In a separate section labeled "Intent," the parties agreed that these indefinite escalator clauses were included in the contracts "for the purpose of compensating [ERG] for the anticipated increase in its operating costs and for the anticipated increase in the value of its Natural Gas to be sold hereunder." J.S. App. 70a.

The contracts also require KPL to make application to the Kansas Corporation Commission ("KCC") for approval of any pass-through to consumers of increased costs arrived at under the price redetermination or the government pricing clause. If a pass-through is not

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[4] Kansas Legislative Research Dep't, *Minutes, Hearings Before the [Kansas] Special Comm. on Energy and Natural Resources* (May 10, 1979) (*"Minutes, Special Comm. Hearings"*) (attached statement of Daryl Smette, Manager, Oil & Gas Sales, ERG at 2).

[5] Indefinite price escalator clauses, which take various forms, generally call for the escalation of a contract price upon and according to the happening of specified contingencies not within the control of the parties to the contract. See generally *Pennzoil Co.* v. *FERC*, 645 F.2d 360, 366 & n.5 (5th Cir. 1981), *cert. denied*, 50 U.S.L.W. 3547 (U.S. Jan. 11, 1982) (No. 81-340); 4 H. Williams, *Oil and Gas Law* § .26 (1981). To be distinguished are fixed or definite price escalator clauses, which provide for automatic, specified price increases at specified times. The ERG/KPL contracts contain a fixed escalator clause calling for a price increase of $.02 per Mcf each year, in the absence of a greater escalation under the indefinite escalator clauses.

approved within 60 days of the application, it is deemed to have been denied. KPL may then elect (but is not obligated) to pay the higher price. If KPL refuses to pay the increased price, ERG has the right to terminate the contracts on 30 days' written notice. J.S. App. 69a.

B. The Statutes.

1. *The Natural Gas Policy Act.* The Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. § 3301 *et seq.* (Supp. IV 1980), was enacted on November 9, 1978, and took effect December 1, 1978. Before its enactment, prices charged by producers for intrastate sales of natural gas in Kansas were not subject to any state or federal regulation, while interstate gas prices were regulated under the Natural Gas Act of 1938, 15 U.S.C. § 717 *et seq.* (1976). A major purpose of Title I of the NGPA was to remedy the serious economic distortions perceived by Congress to have resulted from regulation under the Natural Gas Act, particularly the existence of dual interstate and intrastate markets.[6] Congress' goal in Title I was to create a single national market, in part by imposing price controls during an interim period on interstate and intrastate sales of natural gas, leading to complete price deregulation of many categories of natural gas by January 1, 1985.[7]

Title I contains an intricate set of price ceilings, adjusted upward each month, on various categories of natural gas in both the interstate and intrastate markets. Pertinent to this appeal are the price ceilings of §§ 102, 105, and 109 of that title, 15 U.S.C. §§ 3312, 3315, and 3319. Section 102 sets a maximum price for sales of "new" natural gas, as that term is defined in the

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[6] *Maryland* v. *Louisiana*, 451 U.S. 725, 747 n.22 (1981); H.R. Rep. No. 95-496 (pt. 4), 95th Cong., 1st Sess. 3-6, 87-96 (1977); S. Rep. No. 95-436, 95th Cong., 1st Sess. 7-8 (1977); 123 Cong. Rec. H8177 (daily ed. Aug. 1, 1977) (Rep. Dingell).

[7] H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 67-69 (1978).

statute,[8] which price is adjusted upward monthly.[9] Section 105 establishes price ceilings for natural gas such as that at issue here, *i.e.*, intrastate gas that was under contract as of the date of the NGPA's enactment. Under § 105(b)(1), the ceiling in any given month for the instant gas sales is the price permitted under the terms of the contract as the contract existed on November 9, 1978, or the § 102 "new" gas price, whichever is lower. Section 109 establishes a price ceiling, including monthly upward adjustments, for "natural gas which is not covered by any maximum lawful price under any other section" of Title I. The monthly price ceiling under § 102 is always far higher than the ceiling for the same month under § 109.[10]

2. *The Kansas Price Protection Act.* Other gas suppliers in Kansas had intrastate contracts with KPL that

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[8] The definition of "new" gas is in § 102(c), 15 U.S.C. § 3312(c). The gas involved in this litigation does not qualify as "new" gas.

[9] The statute contains a general inflation adjustment factor, set forth in § 101 of the Act, 15 U.S.C. § 3311, which raises on a monthly basis the various natural gas price ceilings within Title I. The adjustment formula for new gas in § 102(b)(2) also takes into account a "real growth" factor set forth in § 102(b)(2)(B), 15 U.S.C. § 3312(b)(2)(B).

[10] For example, when the NGPA took effect on December 1, 1978, the § 102 ceiling was $2.078 per MMBtu, while the § 109 ceiling was $1.630 per MMBtu. 47 Fed. Reg. 17981, 17982 (April 27, 1982). In November 1978, ERG was receiving from KPL $1.77 per Mcf for the gas here at issue. For June 1982, the § 102 ceiling is $3.132, while the § 109 ceiling is $2.187, and ERG is receiving $2.096. *Id.*

The term "MMBtu" when used with respect to natural gas means 1,000,000 British thermal units. MMBtu's measure energy. The term "Mcf" when used with respect to natural gas means 1,000 cubic feet of gas. The term is a measurement of volume. Typically, as a rule of thumb for gas measurement, one Mcf of gas may be taken to contain 1,000,000 British thermal units of energy; thus 1 Mcf equals approximately 1 MMBtu. For purposes of this litigation the terms "Mcf" and "MMBtu" may be used interchangeably.

contained indefinite escalator clauses like those in ERG's contracts. After enactment of the NGPA, these suppliers (including ERG) notified KPL that the price under their contracts had escalated and that, in accordance with § 105(b)(1) of the NGPA, KPL would be required to pay the § 102 price, beginning December 1, 1978. J.S. App. 7a. On December 7, 1978, KPL petitioned the KCC for a pass-through of costs resulting from these price increases, but no action was taken by the Commission within the 60 days required by the contracts, *i.e.*, by February 5, 1979. J.S. App. 8a-10a. KPL did not elect to pay the escalated price. On February 16, 1979, Mesa Petroleum Company, one of KPL's intrastate suppliers, filed suit in Kansas state court seeking a declaration that it properly terminated its contracts in light of KPL's failure to agree to an increased price.

On February 6, 1979, or one day after expiration of the 60-day period during which KPL had to get KCC approval of a rate increase, S.B. 252 was introduced in the Kansas Senate. The bill provided that all indefinite price escalator clauses in Kansas intrastate gas contracts would be inoperative for one year and could be effective thereafter only to raise the contract price at an annual rate of 5.5%—an escalation significantly less than that called for under the escalator clauses at issue. The bill was the subject of a single Senate committee hearing at which KPL submitted the only written testimony in its favor.[11] After that hearing, a legislative research memorandum emphasized that more than half of the projected extra fuel costs in Kansas triggered by the NGPA in its first year would be borne by KPL, and that the KCC had not yet approved KPL's application to pass on these increases to its customers.[12]

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[11] Kansas Legislative Research Dep't, *Minutes, Hearings Before the Senate Comm. on Energy and Natural Resources* (Feb. 28, 1979) (*"Minutes, February 28 Hearing"*) (attached statement of J.G. Williamson, Exec. Vice Pres., KPL).

[12] See Kansas Legislative Research Dep't, *The Effect of the Natural Gas Policy Act (NGPA) of 1978 on Kansas* 15 (March 27,

The Senate committee failed to report on S.B. 252 before the legislature adjourned its regular session on April 7. On April 25, 1979, during a four-day special "veto session" (traditionally held to reconsider bills vetoed by the governor), a *new* bill, H.B. 2680, was introduced.[13] This bill, which was to become the Kansas Price Protection Act, provided in § 4 for the abrogation of indefinite escalator clauses in contracts for the intrastate sale of Kansas natural gas, as follows:

> "[O]n or after December 1, 1978, the price allowed to be paid pursuant to federal legislation or any regulation by an agency implementing such legislation, or the price paid or to be paid for any sale of natural gas in the state of Kansas shall not be taken into account in applying any indefinite price escalator clause contained in any gas purchase contract subject to this act, to the extent that such contract provides for the sale in the state of Kansas, of gas produced within this state which was not committed or dedicated to interstate commerce on November 8, 1978." J.S. App. 60a-61a.

Section 3 made the law applicable only to contracts entered into before April 20, 1977. J.S. App. 60a. Under § 5 (J.S. App. 61a), indefinite price escalator clauses otherwise abrogated by § 4 could be given effect, after March 1, 1979, up to the NGPA's § 109 ceiling, a ceiling not intended by Congress to apply to intrastate gas already under contract and which not only was substantially lower than the § 102 price authorized under

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1979) (estimated cost of all of the indefinite escalator clause increases in Kansas triggered by the NGPA in the first year are as follows: $9 million to KPL, $3.5 million to Northern Natural Gas, $2 to $2.5 million to Kansas Gas Supply, and $2 million to Sunflower Pipeline).

[13] Senate and House Journals, *Proceedings of the Legislature of the State of Kansas*, 1979 Sess. 858 (*"1979 Legislative Proceedings"*).

these contracts, but also was far lower than the prevailing contract price for sales of intrastate gas at that time. See note 10, *supra*; note 32, *infra*. Section 6 exempted natural gas from stripper wells, new reservoirs, and new wells from § 4's coverage after March 1, 1979, J.S. App. 61a-62a, and thus, after that date, prices for gas sold from such wells were allowed to rise under indefinite escalator clauses to the relevant NGPA ceilings, which were the same as or higher than the § 102 ceiling. See, *e.g.*, NGPA §§ 102 (new gas), 108 (stripper-well gas), 15 U.S.C. §§ 3312, 3318; 47 Fed. Reg. 17981 (April 27, 1982). Section 8 of the bill allowed contracting parties to "voluntar[ily] renegotiat[e] . . . price provisions contained in . . . [their] contracts," thereby delegating to private parties the right to circumvent the restrictions otherwise imposed by the legislation. J.S. App. 62a. Under § 11, the legislation would expire on December 31, 1984. J.S. App. 63a.

H.B. 2680 was passed by the Kansas House of Representatives without legislative hearings, but the Senate voted against taking final action on the bill. *1979 Legislative Proceedings, supra* note 13, at 757, 875-76. The legislature adjourned its veto session on April 28. On May 4, 1979, however, a special joint committee of the two houses of the legislature was appointed to study H.B. 2680 further. J.S. App. 71a.

During the special committee's consideration of the bill, it was obvious that KPL was its "main proponent." [14] In the course of hearings, KPL and other proponents stressed that H.B. 2680 would affect KPL more than anyone else, because KPL purchased about 44% of the intrastate gas subject to indefinite escalator clauses and, according to KCC statistics, stood to bear over half the

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[14] Special Comm. on Energy and Natural Resources, *Report on 1979 H.B. 2680—Restriction of the Operation of Indefinite Price Escalator Clauses in Certain Gas Purchase Contracts* (May 14, 1979) ("Committee Report") (minority view). J.S. App. 81a.

projected cost increases in Kansas caused by NGPA-triggered escalations.[15] Without mentioning that the KCC had not acted upon KPL's December 7, 1978 request to pass on its increased costs to Kansas consumers, KPL and others argued that H.B. 2680 was needed to protect consumers against price increases. The opponents of H.B. 2680 argued, *inter alia*, that it would severely impair existing contractual obligations and that "the [b]ill [was] effectively designed as special legislation for the benefit of a particular utility [KPL] . . . ." [16]

The special committee recommended enactment of H.B. 2680 by a narrow margin of 17 to 15. While the purported intent of the statute was "to minimize the impact on consumers of natural gas price increases," J.S. App. 75a, statistics cited in the majority report showed that the legislation's reach would be quite limited. Since § 4 of the bill would restrict only indefinite escalator clauses in intrastate contracts, its controls would apply to no more than six percent of the natural gas produced in Kansas, or no more than ten percent of the gas consumed in Kansas. J.S. App. 73a.[17] These figures are further

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[15] In 1978, approximately 50 billion cubic feet ("Bcf") of intrastate gas used in Kansas was purchased under contracts having indefinite escalator clauses; KPL purchased 22 Bcf of intrastate gas under such contracts. Kansas Energy Office and Kansas Corporation Comm'n, *Background Memorandum on H.B. 2680*, at 6 (May 8, 1979). If required to pay the escalated price under its contracts, KPL stood to bear over half of the increases borne by the four principal purchasers combined. *Id.* See also *Minutes, Special Comm. Hearings, supra* note 4 (May 9, 1979) (attached statement of David Black, Vice-Pres., KPL).

[16] *Minutes, Special Comm. Hearings, supra* note 4 (May 11, 1979) (attached statement of Dale Stuckey at 12, representing Southwest Kansas Royalty Owners Association).

[17] According to the Committee Report, 866.6 billion cubic feet ("Bcf") of natural gas was produced in Kansas in 1978, and 566.6 Bcf was consumed in Kansas in 1975. In 1978, only 50 Bcf of intrastate gas (both produced and used in Kansas) was subject to indefinite escalator clauses. J.S. App. 73a. Thus less than six percent of the Kansas gas produced in 1978, and (even on the

reduced, moreover, by the many exceptions in H.B. 2680 —for contracts entered into after April 20, 1977 (§ 3); for new gas and stripper well gas (§ 6); and for contracts renegotiated by the parties (§ 8). Thus, the committee's majority acknowledged that the legislation, if passed, would only "provide a *modicum* of restraint on *some* utility price increases." J.S. App. 75a. (emphasis added).

The special committee's 15 minority members opposed the legislation because it would effect a major departure from prior state policy of nonregulation of intrastate gas prices, J.S. App. 80a, and because any possible advantage of the legislation—affecting at most 50 billion cubic feet ("Bcf") out of Kansas' total gas production of 866.6 Bcf—was not worth its severe disadvantages. J.S. App. 82a-84a. Even assuming that fuel cost increases would be passed on to consumers by the KCC, the minority predicted that the artificially depressed price would encourage wasteful use of gas as boiler fuel by KPL's many industrial customers.[18] J.S. App. 81a-82a. The minority also objected that the bill was "designed primarily to support the contention of KPL in its contract dispute with Mesa Petroleum Co., which [was then] being litigated in Grant County District Court." J.S. App. 83a.

On May 14, 1979, the bill was both approved by the special committee and enacted, with amendments not relevant to this dispute, by the two houses of the Kansas legislature in a one-day, wrap-up session. Though the bill was passed by substantial margins, there were mis-

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conservative assumption that natural gas consumption did not increase from 1975 to 1978) less than ten percent of the Kansas gas consumed in state was subject to indefinite price escalator clauses.

[18] KPL sells "approximately 69 percent of its gas to industrial customers, other utilities, and to itself for use in the generation of electricity," not to residential consumers, and uses much of the gas as boiler fuel, which is an "inappropriate and inefficient" use. J.S. App. 81a-82a.

givings about its purpose and effect even among those who voted for it.[19] The statute took effect upon its publication on May 29, 1979, though its regulation of existing contracts reached back to alter contracts executed prior to April 20, 1977, and the prices thereunder to which producers were entitled on or after December 1, 1978.[20]

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[19] Kansas Senators voting against H.B. 2680 inserted comments in the Senate Journal explaining their vote, each noting that "HB 2680 may have been designed primarily to support the contention of KPL in its contract dispute with Mesa Petroleum Co. which [was then] being litigated in Grant County District Court." *1979 Legislative Proceedings, supra* note 13, at 790 (Sen. Sowers); see *id.* at 788-89 (Sen. Angell, co-Chair of the Special Comm.); *id.* at 791 (Sen. Winters). While the Senate ultimately voted 36 to 3 in favor of the bill, *id.* at 787, some of the bill's supporters noted that they did so "reluctantly," bowing to the intense pressure campaign for what they considered "ill-conceived economic policy." *Id.* at 789-90 (Sens. Hein & Morris). In the House, H.B. 2680 passed by a vote of 92 to 31. *Id.* at 973.

[20] Section 4's prohibition was made retroactive to December 1, 1978; and the limited exceptions to § 4 (contained in §§ 5 and 6) did not take effect until March 1, 1979. The March 1, 1979 date was used in §§ 5 and 6, because the Kansas statute was "quite literally copied from [an] Oklahoma law [that] fit Oklahoma circumstances." J.S. App. 84a. The Oklahoma statute, enacted in March 1979, used the March 1, 1979 date. Okla. Stat. Ann., tit. 52, § 260.1 *et seq.* (West Supp. 1982). The Kansas legislature did not change this Oklahoma date even though the Price Protection Act went into effect on May 29, 1979.

Constitutional challenges to the Oklahoma statute are currently pending. *Energy Consumers & Producers Ass'n* v. *Baker*, No. 79-320-D (W.D. Okla., filed Mar. 20, 1979); *Oklahoma Independent Petroleum Ass'n* v. *Baker*, No. 79-823-D (W.D. Okla., filed July 20, 1979) (consolidated with No. 79-320-D). The minority report of the Kansas special legislative committee contended that the Oklahoma statute was unsuitable for Kansas because the volume of intrastate gas affected by indefinite escalator clauses was nearly eight times greater in Oklahoma than was the case in Kansas. J.S. App. 82a, 84a.

C. This Litigation.

1. *ERG's Contract Claims.* On November 20, 1978, ERG notified KPL that, by virtue of the NGPA, the government pricing provisions of the contracts had been triggered and, beginning December 1, 1978, KPL would be required to pay the December 1978 § 102 price of $2.078 per MMBtu, rather than the $1.77 per Mcf price KPL had been paying. J.S. App. 7a. When the KCC failed to approve KPL's request to pass the costs through to its customers within the 60-day period specified by the contracts, J.S. App. 8a-10a, KPL refused to pay the increased price. In June 1979, ERG notified KPL that the contracts were terminated. J.S. App. 10a. KPL denied that ERG had a right to terminate, on the grounds that (1) the government pricing clause was not triggered by the NGPA and (2) the recently passed Kansas Price Protection Act prohibited the operation of that clause. J.S. App. 10a. On July 24, 1979, after KPL's refusal to terminate, ERG requested a price increase to the NGPA § 102 level pursuant to the price redetermination clause. KPL did not dispute ERG's contention that this latter clause would, consistent with the NGPA, trigger an obligation to pay the § 102 price, but it nevertheless contended that its obligation to pay the higher price was extinguished by the prohibition within § 4 of the recently enacted Kansas Price Protection Act. *Id.*

2. *The Decision of the Trial Court.* On July 2, 1979, ERG sought a declaratory judgment from the district court of Harper County, Kansas that its termination of its contracts with KPL was proper. J.S. App. 10a. The issues now before this Court were joined and fully briefed before the trial court on cross-motions for summary judgment in which ERG contended, *inter alia*, that the Kansas statute was invalid under the Contract Clause and that ERG therefore was entitled, under its escalator clauses,

to raise the price to the NGPA § 102 ceiling. J.S. App. 10a, 27a.

The trial court denied ERG's motion and granted KPL's cross-motion for summary judgment. It first ruled that the parties did not intend the government pricing clause to be trigged by enactments such as the NGPA. J.S. App. 27a-28a. On the assumption that an increase under the price redetermination clause would take place but for the Kansas Price Protection Act, J.S. App. 33a-34a, 40a, the trial court concluded that it was "unable to resolve this controversy in a manner that avoids the constitutional issue." J.S. App. 34a. It ruled that the Kansas statute prohibited a price increase under the redetermination clause so that ERG had no cause for termination; and, relying exclusively upon the majority committee report accompanying the legislation and failing to acknowledge the limited reach of the statute, it sustained the Act's constitutionality by finding that it was a reasonable measure with a "legitimate public purpose." J.S. App. 34a-41a.

3. *The Decision of the Kansas Supreme Court.* The Kansas Supreme Court affirmed. It disagreed with the trial court's rationale as to why there could be no increase under the government pricing clause. The court held that "the parties *intended* that the government price escalation clauses be triggered by enactments such as the NPGA," J.S. App. 14a (emphasis in original), but that § 105(b)(1) of the NGPA precluded any escalation under that clause. In considering the effect of the Kansas Price Protection Act on the price redetermination clause, the Supreme Court affirmed the trial court's decision applying the Kansas statute to prohibit a price increase or termination of the contracts. J.S. App. 15a-22a. The court adopted verbatim the trial court's reasoning on the constitutional question. J.S. App. 16a-22a.[21]

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[21] The court below did not expressly consider the effect of the Kansas Price Protection Act on the government pricing clause, because of its ruling that escalation under that clause was barred

SUMMARY OF ARGUMENT

But for the Kansas Price Protection Act, ERG would have been entitled, under the price redetermination clause, either to the escalation of its contract price price up to the NGPA § 102 ceiling or, upon KPL's refusal to pay the § 102 price, to termination of the contracts. Section 4 of the Kansas Price Protection Act, as construed by the Kansas Supreme Court, deprives ERG of those contractual rights. Moreover, as we show below (pp. 17-18, *infra*), ERG was entitled under its government pricing clause to receive from KPL the § 102 price beginning December 1, 1978, and § 4, which became effective May 29, 1979, reached back to extinguish that obligation as well. Under the test enunciated in *Home Building & Loan Association* v. *Blaisdell*, 290 U.S. 398 (1934), and recently reaffirmed and applied in *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234 (1978), and *United States Trust Co.* v. *New Jersey*, 431 U.S. 1 (1977), the Kansas Price Protection Act violates the Contract Clause of Article I, Section 10, of the Constitution because it (a) works a substantial impairment of contractual obligations, (b) does not address an important general social problem, and (c) is not (i) a necessary and (ii) a reasonable means to achieve the statute's ostensible purpose.

(a) The statute's severe restriction of ERG's escalation rights was clearly a substantial impairment of contract. ERG would never have entered into these long-term, "life-of-the-field" contracts without assurance that it would be fully compensated for future increases in the value of its product. Indeed, the escalator clauses were expressly included in these agreements to "compensat[e]

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in any event by § 105(b)(1) of the NGPA. See p. 14, *supra*. The court did not limit its Contract Clause rationale, however, to the Kansas statute's application to the price redetermination clause, but discussed and sustained the constitutionality of the statute's restrictions upon indefinite escalator clauses in general.

[ERG] for . . . the anticipated increase in the value of its Natural Gas to be sold" under the contracts. J.S. App. 79a. This was not a "minimal contractual interest," as the court below thought. J.S. App. 18a. The escalator clauses were the very "heart of the obligation," *United States Trust*, 431 U.S. at 41, and ERG "was substantially induced to enter into these contracts on the basis of" KPL's promise to pay the contract price, as adjusted through these provisions. *City of El Paso* v. *Simmons*, 379 U.S. 497, 514 (1965).

(b) The Kansas statute does not address "an important general social problem." *Allied Structural Steel*, 438 U.S. at 247. By virtue of its narrow focus and many exceptions, the statute imposes "controls" on only a fraction of Kansas' intrastate natural gas sales. Even the modest amount of gas affected is subject to a major statutory loophole which permits the contracting parties to "voluntar[ily] renegotiate . . . price provisions contained in [their] . . . contracts." J.S. App. 62a. Accordingly, proponents of the statute could say only that it "would provide a *modicum* of restraint on *some* utility price increases." J.S. App. 75a (emphasis added). On the other hand, the legislation was of enormous benefit to its principal sponsor, KPL, which freely acknowledged to the Kansas legislature that more than half of the projected cost increases in Kansas resulting from the triggering of indefinite price escalator clauses by the NGPA could be traced to KPL's own contracts.

(c) In any event, "without modifying the [contract] at all, the State[] could have adopted alternative means of achieving [its] goal[]" of protecting consumers from utility price increases. *United States Trust*, 431 U.S. at 29-30. There were clearly alternative means available to the Kansas legislature to achieve its ostensible goal, the most obvious of which would have been to prohibit all or part of the pass-through to consumers of the cost increases resulting from KPL's contractual obligations. The legislature in enacting the statute at issue created a false

dichotomy insofar as it assumed that it had to side with either producers or consumers in this instance. It is obvious that KPL should have to bear a major responsibility for any of the price increases, since that utility executed these contracts knowing full well that rising natural gas prices were in the offing.

Nor is the Kansas statute a reasonable measure for accomplishing the legislature's ostensible purpose. Its limited scope and abundant exemptions insure that it could not begin to solve the problem of rising utility costs in Kansas. The statute is also unreasonable because it lacks the temporary character found so important in *Blaisdell*. 290 U.S. at 440, 445; see *Allied Structural Steel*, 438 U.S. at 242. ERG is required to sell its gas to KPL at a price far below market value from December 1, 1978, through December 31, 1984; ERG will *never* recoup these losses.

For these reasons and others outlined in our argument, the Kansas Price Protection Act should not be sustained by this Court.

2. The natural gas involved here is governed by § 105(b)(1) of the NGPA, which sets a ceiling price of either the price provided for "under the terms of the existing contract, . . . as such contract was in effect on [November 9, 1978]," or the § 102 price, whichever is lower. The statute by its terms thus looks to the entire *contract*, and not the *price*, in effect on November 9, 1978. Section 105's legislative history and its construction by two federal courts of appeals and by FERC make clear that the reference in § 105(b)(1) to "the price under the terms of the existing contract" as such contract was "in effect on" November 9, 1978 does *not* mean the November 9, 1978 "contract price"; it means, instead, the price to which a producer is entitled at any point in time under, *inter alia*, indefinite escalator clauses in existence on November 9, 1978. Thus, if one of the "terms" of a contract is a government pricing clause (such as ERG's) which provides for an automatic price

increase to the highest level permitted by law, and if that clause was in effect on November 9, 1978, the price would escalate under § 105(b)(1) in accordance with that clause, up to the § 102 ceiling for any given month.

The Kansas Supreme Court misconstrued § 105(b)(1), however, by reading that provision's reference to the "price under the terms of the existing contract" as of November 9, 1978 to mean "the November 9th gas price." J.S. App. 14a. Since the court found that ERG's November 9, 1978 price "was lower than the Section 102 price" for December 1978 (and, implicity, for every month thereafter), it erroneously ruled that the government pricing clause "did not escalate." *Id.* That misinterpretation of this critically important provision of the NGPA should be corrected by this Court.

ARGUMENT

I. THE KANSAS PRICE PROTECTION ACT WORKS A SUBSTANTIAL IMPAIRMENT OF THE OBLIGATION OF CONTRACTS IN A MANNER VIOLATIVE OF ARTICLE I, SECTION 10 OF THE UNITED STATES CONSTITUTION.

The principal question presented on this appeal is whether the Kansas Price Protection Act abridges the Contract Clause of Article I, Section 10 of the United States Constitution.[22] That Clause provides that "[n]o

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[22] The constitutional question presented herein cannot be avoided by resolution of the statutory question. This is because the Kansas Supreme Court's ruling on § 105(b)(1) of the NGPA by its terms applies only to the government pricing clause of the contracts, not to the wholly independent price redetermination clause. The Kansas Supreme Court found that it could not deny ERG's claim under the latter contractual provision without relying on the Kansas Price Protection Act and upholding its constitutionality. J.S. App. 16a. Thus, even if this Court should leave standing the Kansas court's ruling that the price could not escalate under the government pricing clause, it would have to reach the constitutional issue with respect to the price redetermination clause. Conversely, if this

state shall . . . pass any . . . Law impairing the Obligation of Contracts . . . ." While the "prohibition is not an absolute one and is not to be read with literal exactness," *Home Building & Loan Association* v. *Blaisdell*, 290 U.S. 398, 428 (1934), it does impose restraints on the authority of a State "to abridge existing contractual relationships, even in the exercise of its otherwise legitimate police power." *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234, 242 (1978); see *id.* at 244. Indeed, in its two most recent Contract Clause decisions, *Allied Structural Steel* and *United States Trust Co.* v. *New Jersey*, 431 U.S. 1 (1977), this Court reaffirmed the vitality of the Clause in striking down state laws far less objectionable than the legislation here.[23]

The decision below conflicts with this Court's recent decisions interpreting the Contract Clause and with the

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Court reverses the Kansas Supreme Court on § 105(b)(1), thereby allowing escalation under the government pricing clause as far as federal statutory law is concerned, the Kansas courts undoubtedly would apply the Price Protection Act to bar escalation under the government pricing provision, see note 21 *supra*—an argument KPL has advanced throughout this litigation.

[23] Even before this Court's recent decisions in *United States Trust* and *Allied Structural Steel*, state supreme courts were vigilant in enforcing the Contract Clause to invalidate state laws abrogating escalation provisions in pensions and other contracts involving rights to compensation. See *Yeazell* v. *Copins*, 402 P.2d 541 (Ariz. 1965) (*en banc*); *Bardens* v. *Board of Trustees of Judges Retirement Sys.*, 174 N.E.2d 168 (Ill. 1961); *Campbell* v. *Michigan Judges Retirement Bd.*, 143 N.W.2d 755 (Mich. 1966); *Sylvestre* v. *State*, 214 N.W.2d 658 (Minn. 1973); *Eisenberger* v. *Police Pension Comm'n of Harrisburg*, 162 A.2d 347 (Pa. 1960); *Bakenhus* v. *City of Seattle*, 296 P.2d 536 (Wash. 1956) (*en banc*). Laws limiting escalation provisions have continued to receive rigorous state court scrutiny following this Court's recent Contract Clause analysis. See *Wagoner* v. *Gainer*, 279 S.E.2d 636 (W.Va. 1981); *Olson* v. *Cory*, 636 P.2d 532 (Cal. 1980); *Sonoma County Org. of Public Employees* v. *County of Sonoma*, 591 P.2d 1 (Cal. 1979) (*en banc*); *Miles* v. *Tennessee Consol. Retirement Sys.*, 548 S.W.2d 299 (Tenn. 1976).

Court's earlier precedents, including the leading case of *Home Building & Loan Association* v. *Blaisdell*, *supra*. The Kansas courts uncritically supposed a legitimate purpose on the part of the Kansas legislature even though such a purpose clearly is belied by the statute's plain terms, impact, and legislative history. Each of these factors demonstrates that the hastily adopted Price Protection Act had the principal effect of relieving KPL, one of the State's largest utilities, of its obligations under otherwise valid long-term natural gas purchase contracts, while controlling the price of only a fraction of the natural gas produced or used in Kansas.

If generally applied, the Kansas Supreme Court's reasoning would permit States to enact special legislation designed to relieve powerful constituencies of significant contractual obligations on the basis of unfounded, broad assertions of the public benefits to be derived from the enactment, with utter indifference to the legitimate interests of the other parties to the contract.[24] If such legislation is sustained, then the Contract Clause will be, contrary to what this Court has said, "a dead letter." *Allied Structural Steel*, 438 U.S. at 241.

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[24] Indeed, the Contract Clause was included in the Constitution because of the Framers' strong disapproval of widespread retroactive state legislation altering private contracts in the pre-Constitution period. See generally *Home Building & Loan Ass'n* v. *Blaisdell*, 290 U.S. 398 (1934); 2 B. Schwartz, *A Commentary on the Constitution of the United States: The Rights of Property* 266 *et seq.* (1965); B. Wright, *The Contract Clause of the Constitution* (1938). The Clause was intended by the Framers to prohibit "laws which altered the obligations of contracts by effectively relieving one party of the obligation to perform a contract duty." *Allied Structural Steel*, 438 U.S. at 257 (Brennan, J., dissenting). To guard against such special interest laws, the Contract Clause was included as an "added . . . constitutional bulwark in favor of personal security and private rights." *The Federalist*, No. 44, at 301 (J. Cooke ed. 1961).

A. The Kansas Price Protection Act Works a Severe and Substantial Impairment of Contractual Obligations.

In Contract Clause analysis, "the first inquiry must be whether the state law has, in fact, operated as a substantial impairment of a contractual relationship." *Allied Structural Steel*, 438 U.S. at 244. It is clear that there was such an impairment here, since the Price Protection Act substantially modifies and devalues the central term of these life-of-the-field contracts—the price term. This surely was not a "minimal contractual interest," as the Kansas courts thought. J.S. App. 18a, 36a. Rather, it goes to the very "heart of the obligation." *United States Trust*, 431 U.S. at 41.[25]

Clearly, "the price provisions are the most important provisions in any gas contract." [26] The increased demand for gas in the post-World War II years and the corresponding desire of purchasers to have assured sources of supply has resulted in buyer pressure on gas producers to enter into long-term contracts. Faced with this demand and with rising costs, as well as an overall but erratic inflationary trend, many gas producers have sought safeguards through indefinite price escalator provisions in such long-term contracts.[27] As the Tenth Circuit recently said, indefinite price escalator clauses " 'are a common feature of [intrastate] gas purchase and sale contracts' "

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[25] *Cf. Somona County Org. of Public Employees* v. *County of Somona*, 591 P.2d 1, 7 (Cal. 1979) (*en banc*) (provision for wage escalation "is frequently the very heart of an employment contract," since employees would give up other benefits in return for guaranteed escalation).

[26] Taylor, *Escalation Clauses in Gas Purchase Contracts*, 3 Alberta L. Rev. 255, 255 (1964).

[27] Gregg, *Negotiating & Drafting Gas Purchase Contracts on Behalf of the Seller*, Thirteenth Annual Institute on Oil and Gas Law and Taxation 87 (1962). See also E. Neuner, *The Natural Gas Industry* 265-66 (1960); 4 H. Williams, *Oil and Gas Law* § 726, at 748.4 to 748.5 (1981).

because of purchasers' demands for long-term commitments and producers' needs for assurance that they will receive the market price, over time, for their product.[28]

The parties to this appeal are not in dispute that, in the absence of the Price Protection Act, ERG's "[price] redetermination clause would have authorized escalation of the contract price up to the NGPA § 102 new gas price."[29] Yet § 4 of the Kansas Price Protection Act deprives ERG of its contractual right to the § 102 price. Moreover, as we show in Part II (pp. 42-48, *infra*), ERG was entitled, beginning December 1, 1978, to receive from KPL the § 102 price under the government pricing clause; and § 4, which went into effect on May 29, 1979, reached back to abrogate that contractual obligation. While § 5 of the Kansas statute allows escalation of prices after March 1, 1979 to the ceiling set by § 109 of the NGPA, the latter ceiling was not intended by Congress to apply to the intrastate gas involved here, but only to gas not under contract when the NGPA was adopted, and the § 109 ceiling is substantially lower than the § 102 ceiling, which *was* intended by Congress to govern sales of the gas in controversy.

Thus, the contract price ERG received on December 1, 1978 was $1.79 per Mcf, while the § 109 price for that month was only $1.630 and the § 102 price was $2.078.[30]

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[28] *Kerr-McGee Corp.* v. *Northern Utilities, Inc.*, 673 F.2d 323, 327 (10th Cir. 1982) (quoting *Amoco Prod. Co.* v. *Stauffer Chem. Co.*, 612 P.2d 463, 468 (Wyo. 1980)); see *Texas Gas Transmission Corp.* v. *Shell Oil Co.*, 363 U.S. 263 (1960); *Superior Oil Co.* v. *Western Slope Gas Co.*, 604 F.2d 1281 (10th Cir. 1979).

[29] Brief of *Amicus Curiae* State Corporation Commission of the State of Kansas in Support of Appellee's Motion to Dismiss at 5 ("KCC Br. *Amicus Curiae*"); see KPL Motion to Dismiss at 6-7.

[30] A schedule of NGPA ceiling prices for each month from December 1978 to July 1982 may be found in 47 Fed. Reg. 17981 (April 27, 1982). Appended to this brief is a summary chart of the §§ 102

The § 109 price remained low for so long that it did not reach the contract price KPL was paying ERG until April 1980.[31] Three years after the NGPA's enactment, when the § 102 price was $2.94, KPL was only paying ERG $1.83 for the gas here at issue.[32]

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and 109 prices taken from this comprehensive schedule, as well as the price that has been paid by KPL to ERG for the same period of time.

A small percentage of ERG's gas under contract to KPL qualifies as "stripper well" gas and thus brings a higher price under § 108 of the NGPA and § 6 of the Kansas Price Protection Act. That gas is not at issue on this appeal.

[31] In a separate pending action, KPL has contended that under the price redetermination clause, ERG is entitled only to an escalation up to the § 109 ceiling in effect on the date of the redetermination, which redetermined price then remains in effect for the full two years until the next redetermination, without subsequent monthly increases in price allowed by § 109. *The Kansas Power & Light Co.* v. *Energy Reserves Group, Inc.*, No. 81-C-13 (Harper County, Kansas Dist. Ct.). Under KPL's theory, ERG could not obtain the benefit of the § 109 price as soon as it exceeded the contract price in April 1980, but would have to wait until the next price redetermination in November 1981.

[32] The inappropriateness of applying the low § 109 price to the gas here at issue is further evidenced by the NGPA's statutory scheme relating to ceilings for intrastate gas under contract when the NGPA was enacted. The ceilings were set in each instance at or above the existing contract price (with provision for monthly escalation), see NGPA §§ 105(b)(1), (2), 106(b), 15 U.S.C. §§ 3315(b)(1), (2), 3316(b), so as to preserve the "sanctity" of intrastate gas contracts. See Staff of the House Comm. on Interstate and Foreign Commerce and the Senate Comm. on Energy and Natural Resources, 95th Cong., 2d Sess., *Natural Gas Pricing Agreement Adopted by the Conferees on H.R. 5289*, at 18 (Comm. Print 1978) (*"Conference Pricing Agreement"*). The § 109 ceiling applied to intrastate gas *not* subject to an existing contract on the date of enactment, NGPA § 109(a)(3), 15 U.S.C. § 3319(a)(3), reflecting a judgment that the low § 109 ceiling should be applied *only* when contract rights and expectations would not be affected.

Indeed, Congress balked at a proposal by the Carter Administration that would have modified existing intrastate gas contract prices. "This action is indefensible," stated Senator Tower. "Exploration and development programs have been budgeted and other

In short, "a basic term of the . . . contract—one on which the company had relied for [many] years—was substantially modified." *Allied Structural Steel*, 438 U.S. at 246. It is not true, as the courts below maintained, that the Kansas statute merely prevents ERG from "'reap[ing] unanticipated, windfall financial benefits.'" J.S. App. 18a, 36a (quoting Committee Report, *supra* note 14, at 4 (J.S. App. 74a)). ERG relied heavily on the inclusion of provisions for price escalation when it agreed to commit all of its gas production from the Spivey-Grabs field to KPL over the entire life of the field and its associated processing plant. The "Intent" clause of the contracts makes that plain.[33] When the parties entered into the contracts in September 1975, prices of natural gas (like other energy sources) already were rising,[34] and ERG agreed to a lower initial contract price

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investment decisions made on the basis of the current or anticipated stream of revenues available to producers under intrastate sales contracts. In such situations, the administration assures a cutback in drilling activity." 123 Cong. Rec. S15337 (daily ed. Sept. 22, 1977); see *id.* at S15350 (Sen. Stone); *id.* at S15536 (daily ed. Sept. 24, 1977) (Sen. Bentsen). See also *id.* at H8191 & H8317 (daily ed. Aug. 1 & 2, 1977) (Rep. Brown). For this and other reasons, Congress did not adopt the Administration's approach and, under § 105, established price ceilings applicable to contracted-for intrastate gas at or above the § 102 level. *Conference Pricing Agreement, supra*, at 18.

[33] In these contracts, ERG and KPL expressed their intent that the purpose of the price escalation provisions was to "compensat[e] [ERG] for the anticipated increase in its operating costs and for the anticipated increase in the value of its Natural Gas to be sold" under the contracts. J.S. App. 70a. ERG identified changes in government regulation as one of the eventualities that could trigger a price increase. J.S. App. 66a. Further, ERG anticipated that KPL might refuse to pay increased prices if it could not pass them on to its customers, and therefore preserved for itself the option to terminate the contracts in that event. J.S. App. 69a.

[34] See, *e.g.*, Staff of Subcom. on Energy, Joint Economic Comm. of Congress, 95th Cong., 1st Sess., *The Economics of the Natural Gas Controversy* 18-19 (Joint Comm. Print 1977) (Tables 4 and 5). KPL itself admits that most of its contracts containing

only because KPL agreed to include these indefinite escalator clauses so as to insure that ERG would be fully compensated for the value of the gas over the entire term of the contract. See note 4, *supra*. Moreover, when these contracts were executed, Congress had before it several gas deregulation proposals, the broadest of which was passed by the Senate a month later.[35]

This sequence of events demonstrates that there was a real prospect at the time of contracting that increases would be triggered by higher prices for gas. When these parties entered into long-term supply contracts with escalator clauses, they had every expectation that the price would continue to go up in the years to come. Thus, the Kansas Price Protection Act did not "restrict a party to those gains reasonably to be expected from the contract," *City of El Paso*, 379 U.S. at 515, but deprived ERG of its reasonably expected gains and bestowed a substantial windfall on KPL.[36]

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indefinite price escalator clauses "or the supplements to them are 1975 or later. About this time the producers became aware, as I'm sure we did, too, that there was in the horizon, the foreseeable horizon, some increasing prices in the cost of gas." Transcript of Hearing in Docket No. 118, 447-U, at 45 (KCC May 2, 1979) (testimony of J.G. Williamson, Exec. Vice-Pres., KPL).

[35] Early in 1975, the Ford Administration proposed deregulation of interstate gas, and its proposal was introduced in the Senate as S. 594. 121 Cong. Rec. 2448 (Feb. 5, 1975). The Senate Commerce Committee reported a more limited bill (S. 692) which allowed higher prices for new gas, *id.* at 18525 (June 12, 1975), and an emergency measure (S. 2310) permitting temporary increases in interstate gas was put on the Senate calendar in early September. *Id.* at 28090 (Sept. 9, 1975). S. 2310 was amended to include provision for permanent deregulation of new gas sold interstate and, after lengthy debate in late September and October, was passed in the Senate by a vote of 58-32. *Id.* at 33655 (Oct. 22, 1975).

[36] The KCC has argued that ERG's expectations here were limited by a clause in the contracts which provides that the contracts are subject to "all relevant present and future state and federal laws."

Moreover, the producers of gas in Kansas relied on these escalator provisions in making production decisions. Producers were willing "to drill and complete new wells knowing that [they] would be receiving the highest market price for [their] gas. Without these clauses and without this protection many . . . wells would not have been drilled."[37] Consequently, "[n]ot only did the state law thus retroactively modify the compensation that the company had agreed to [receive] . . . but also it did so by changing the company's obligations in an area where the element of reliance was vital." *Allied Structural Steel*, 438 U.S. at 247.

J.S. App. 69a; KCC Br. *Amicus Curiae*, *supra* note 29, at 6-7. This would be the case even without any explicit acknowledgment; but it is obvious that the contracts are subject only to state or federal laws that are *valid*. ERG claims that the Price Protection Act is not. "An unconstitutional law is void, and is as no law." *Ex parte Siebold*, 100 U.S. 371, 376 (1879).

In any event, the contractual provision upon which the KCC relies also states that ERG retains its right to terminate the contracts if it fails to receive bargained-for price escalations because of a change in applicable law. J.S. App. 69a-70a. Thus, this provision does not contemplate that measures, such as the statute at issue, would abrogate ERG's termination rights and there can therefore be no doubt than that ERG's contract rights were impaired by the Price Protection Act. *But cf. Edmiston* v. *State Corp. Comm'n*, No. 79-1335, slip op. (D. Kan. Nov. 24, 1980), *as modified*, *id.* 36 (D. Kan. Jan. 13, 1981) (upholding the Kansas Price Protection Act), *appeal docketed*, No. 81-1197 (10th Cir. Feb. 23, 1981) (oral argument postponed after probable jurisdiction was noted in this case).

[37] *Minutes, Special Comm. Hearing*, *supra* note 4 (May 10, 1979) (attached statement of Roger McCoy, McCoy Petroleum, Inc. at 1, 2); see *id.* (attached statement of Mesa Petroleum Co.). The same point was made in the Senate hearing on S.B. 252. "Many marginal gas wells now being produced at little or no profit in expectation of higher prices from triggering of price escalator clauses will be plugged out. In that event, the natural gas production from these wells will be lost forever." *Minutes, February 28 Hearing*, *supra* note 11 (attached statement of R.D. Randall, objection 4). See also *id.* (attached statement of Donald Schnacke, objection 4).

In sum, ERG would not have entered into these long-term, "life-of-the-field" contracts, under which it committed a large part of its natural gas for an indefinite period of time, without the assurance that it would be fully compensated for future increases in the value of its product. The payment obligations to which KPL agreed, including those under the indefinite price escalator clauses, were KPL's "central undertaking" and were "the primary consideration for" ERG's agreement to assure KPL its long-term supply of natural gas. *City of El Paso*, 379 U.S. 514. ERG "was substantially induced to enter into these contracts on the basis of" KPL's promise to pay the contract price, as adjusted through the escalator provisions. *Id.* Modification of these escalation rights constituted a severe, substantial impairment of these contracts.

B. The Statute Does Not Address an Important General Social Problem and, in Any Event, Would Be an Unnecessary and Unreasonable Means Even to a Legitimate End.

In considering whether a state's impairment of contractual obligations is constitutional, the "height of the hurdle the state legislation must clear" is determined by the degree of impairment. *Allied Structural Steel*, 438 U.S. at 245. Severe impairment, as in this case, "will push the inquiry to a careful examination of the nature and purpose of the state legislation." *Id.* This Court's examination has focused on the five factors considered significant by the *Blaisdell* Court,[38] whose opinion "clearly

[38] "First, the state legislature had declared in the Act itself that an emergency need for the protection of homeowners existed. [290 U.S.] at 444. Second, the state law was enacted to protect a basic societal interest, not a favored group. *Id.*, at 445. Third, the relief was appropriately tailored to the emergency that it was designed to meet. *Ibid.* Fourth, the imposed conditions were reasonable. *Id.*, at 445-447. And, finally, the legislation was limited to the duration of the emergency. *Id.*, at 447." *Allied Structural Steel*, 438 U.S. at 242.

implied that if the Minnesota moratorium legislation [upheld in *Blaisdell*] had not possessed the characteristics attributed to it by the Court, it would have been invalid under the Contract Clause of the Constitution." *Allied Structural Steel*, 438 U.S. at 242.

Rather than engage in careful scrutiny of the Kansas statute to determine if each of the *Blaisdell* characteristics was present, the court below uncritically deferred to the legislature's justification for the statute. J.S. App. 18a, 36a. Indeed, the Kansas Supreme Court merely adopted verbatim the statements of the trial court, J.S. App. 16a-22a, which itself had adopted verbatim the statements of the majority of the special committee that recommended the legislation. J.S. App. 36a-37a. As we show below, had the Kansas Price Protection Act been subjected to the careful examination mandated by this Court, it could not have been sustained.

1. *The statute does not address an important general social problem.*

In determining whether the end sought to be achieved by a state legislature justifies the impairment of a contractual obligation, this Court has focused on two criteria: first, whether the legislation was enacted because of a public "emergency" and, second, whether the legislation "was addressed to a legitimate end," that is, whether it was "for the mere advantage of particular individuals [or] for the protection of a basic interest of society." *Blaisdell*, 290 U.S. at 444-45; see *Allied Structural Steel*, 438 U.S. at 248-49.

(a) Here, there was no public "emergency" or "crisis" declared by the Kansas legislature, as there was in *Blaisdell* and other cases upholding legislative modification of contracts.[39] The increasing cost of energy was hardly a

[39] The Kansas Supreme Court in the instant case thought that the Price Protection Act addressed an "emergency situation," J.S. App. 22a, albeit only sketchily described and without reference to

new or unexpected problem in 1979 (see note 34, *supra*), and Kansas had never before regulated prices charged by producers in intrastate sales of natural gas.[40] Moreover, Congress viewed deregulation and the consequential increase in prices as ultimately in the public interest: the higher prices would stimulate further gas exploration and drilling by producers and would encourage natural gas conservation by consumers.[41] A situation considered beneficial to the public by Congress cannot at the same time be deemed a state "emergency" justifying the destruc-

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any legislative finding or statement. In contrast, the state court in *Blaisdell* upheld the statute as an "emergency measure" by reference to a specific legislative declaration of "a state of emergency" which had an "adequate basis." 290 U.S. at 444. See also *East New York Savs. Bank* v. *Hahn*, 326 U.S. 230 (1945) (upholding a statute addressing problems caused by the continuing emergency brought on by the Great Depression).

[40] The presence or absence of previous state regulation has been identified by this Court as a factor to be considered in assessing the constitutionality of a legislative impairment of contractual rights. Compare *Allied Structural Steel*, 438 U.S. at 242 n.13, 249, with *Veix* v. *Sixth Ward Bld'g & Loan Ass'n*, 310 U.S. 32, 38 (1940). While Kansas has in the past regulated non-price features of gas production, see K.S.A. § 55-701 *et seq.* (1976); Kan. Admin. Regs. 82-2-100 to 82-2-800, that is irrelevant to Contract Clause scrutiny since "there is no indication that the particular contractual relationship here involved has, as such, ever been caught up in the general scheme of regulation." *Garris* v. *Hanover Ins. Co.*, 630 F.2d 1001, 1007 (4th Cir. 1980); see *Treigle* v. *Acme Homestead Ass'n*, 297 U.S. 189, 196 (1936).

[41] "[W]hen Congress designed the NGPA, '[t]he balance Congress struck already took into account the conflicting interests of producers and consumers' . . . . Congress was well aware of the economic impact on consumers that would result from the operation of indefinite escalator clauses. The decision to permit contract clauses to raise prices to a ceiling constitutes a clear legislative statement that the resulting high cost to the consumer is not contrary to federal energy policy."

Kerr-McGee Corp. v. *Northern Utilities, Inc.*, *supra* note 28, 673 F.2d at 326-27 (quoting *Pennzoil Co.* v. *FERC*, *supra* note 5, 645 F.2d at 379).

tion of valid contract rights. In short, "[t]his legislation, [causing] a sudden, totally unanticipated, and substantial retroactive [change in the contracts] was not enacted to deal with a situation remotely approaching the broad and desperate emergency economic conditions of the early 1930's—conditions of which the Court in *Blaisdell* took judicial notice." *Allied Structural Steel*, 438 U.S. at 249.

(b) Nor was the Price Protection Act "addressed to a legitimate end" by solving "an important general social problem." *Allied Structural Steel*, 438 U.S. at 247; see *id.* at 242; *Blaisdell*, 290 U.S. at 445. While the Kansas Supreme Court credited the legislature with supposed concern for the effect on consumers of rising utility costs, J.S. App. 18a-19a, 22a, the facts available to both the court and legislature undercut that conclusion. First, less than one-quarter of the gas consumed in Kansas is derived from intrastate sales.[42] Second, the statute affects indefinite, but not fixed, escalator clauses; the former are found in contracts covering less than ten percent of the natural gas consumed in Kansas. See note 17, *supra*. Third, the statute exempts some of the natural gas contracts that otherwise would be within its limited coverage. For example, § 3 limits the Act's coverage to "contracts entered into before April 20, 1977," thereby excluding many contracts containing indefinite escalator clauses. A national survey suggests that gas contracts

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[42] Statistics prepared for the Kansas legislature show that 71% of the residential and commercial requirements for natural gas in Kansas were served by the Cities Service Gas Company, an *interstate* natural gas pipeline company whose contracts therefore are not affected by the Price Protection Act. Cities Service also provides 49% of the natural gas used for the generation of electrical power and industrial and other uses. Kansas Legislative Research Dep't, *supra* note 12, at 3. Consumption of natural gas in Kansas totalled 566.6 Bcf in 1975; even assuming that consumption did not increase at all between 1975 and 1978, the figures before the legislature would have shown that at most 23.8% of the total consumption was provided by intrastate sales. J.S. App. 73a.

entered into after April 20, 1977 are just as likely to contain indefinite escalator clauses as those executed before that date.[43] Fourth, by allowing "voluntary renegotiation of price provisions contained in natural gas purchase contracts," § 8 of the Act entrusts to private parties the final responsibility for enforcing the statute's purported goal of consumer protection.

Given the limited reach of the statute, it is not at all surprising that the most the bill's supporters could say about it was that it "would provide a *modicum* of restraint on *some* utility price increases." J.S. App. 75a (emphasis added). It is clear that the price of natural gas produced or used in Kansas is largely unaffected by the Price Protection Act.

On the other hand, KPL had a great stake in the passage of the statute. It purchased 44% of the Kansas intrastate gas under indefinite escalator clauses, see note 15, *supra*, and stood to pay more than half the total increases in Kansas caused by the NGPA's triggering of such clauses. See note 12, *supra*. It was and still is by no means clear that without the Price Protection Act, price increases ever would be "passed on" to KPL's consumers. ERG's contracts with KPL acknowledge that the KCC may disapprove the pass-on of increased costs of natural gas. J.S. App. 69a; see pp. 4-5, *supra*.[44] In

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[43] Decision Analysis Corp., *Analysis of Natural Gas Producer Interstate Pipeline Contracts* 6-7 (July 1, 1981) (Table 2). Of the 72 randomly sampled post-April 1977 contracts, all but one had indefinite escalator clauses. This was similar to the high percentage for the period January 1973 to April 1977 and well above the percentage for the period before January 1973.

[44] Whether in the absence of the Kansas Act the KCC would have permitted a full pass-through of increased purchased-gas costs due to indefinite escalator clauses is certainly highly problematical, particularly in view of the fact that so much of the gas affected by such clauses in Kansas is under contract to KPL. A leading commentator on utility regulation states the general rule as follows:

fact, KPL's application for a pass-through had been pending before the KCC for over five months before the Price Protection Act was passed.[45]

Even if the KCC would have approved a full pass-through of the price increases, KPL still could have experienced a restriction on its rate of return and a contraction of its rate base as a result of the operation of the indefinite escalator clauses.[46] Whatever KPL may say, obtaining KCC approval of a pass-through would

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"Regulatory agencies may exclude particular outlays from operating expenses (1) if the questioned outlays represent 'inefficiency' or 'improvidence,' or (2) managerial discretion has been abused, or (3) the action taken has been 'arbitrary,' or 'inimical to the public interest,' or (4) there has been 'economic waste,' or (5) such outlays were not legitimate operating expenses because they were 'in excess of just and reasonable charges.'" 1 A. Priest, *Principles of Utility Regulation* 51 (1962).

See also, *e.g.*, *NAACP* v. *FPC*, 425 U.S. 662, 666-68 (1976); *Acker* v. *United States*, 298 U.S. 426, 430-31 (1936).

[45] On November 9, 1979, or over eleven months after KPL first petitioned for a pass-through of increased costs occasioned by the NGPA and almost five and one-half months after the Price Protection Act was passed, the KCC denied KPL's request for a pass-through on grounds that the Price Protection Act barred the increases. App. 5.

[46] KPL has an obligation to "furnish reasonably efficient and sufficient service" at "just and reasonable rates." K.S.A. § 66-107 (1980). Because one-third of KPL's supply contracts contained indefinite escalator provisions (causing KPL to bear more of the costs of gas deregulation than all other purchasers combined), the KCC, in the absence of the Price Protection Act, would have had substantial grounds not only to refuse to allow KPL to pass on to its customers the full increase in purchased-gas costs due to such provisions, but also to reduce KPL's allowable rate of return in connection with future requests for general rate increases. Moreover, escalation of prices to KPL's consumers, especially industrial consumers to which KPL sells nearly 70 percent of its natural gas (see note 18, *supra*), would very probably have restricted demand, thereby reducing KPL's rate base. See P. Starrett, *The Natural Gas Shortage and the Congress* 3 (1974).

not have helped KPL as much as preventing price increases in the first instance.

As the minority report of the legislature's special committee bluntly stated: "the people of Kansas, especially the residential consumers, are the victims of a cruel hoax," for it appeared that the Price Protection Act was "designed primarily to support the contention of KPL in its contract dispute with Mesa Petroleum Co., which is presently being litigated in Grant County District Court. The Legislature should not become involved by taking sides in such contract disputes." J.S. App. 83a-84a. Indeed, it is striking how the Price Protection Act so precisely satisfied KPL's, rather than the public's, pressing needs at the time of that statute's passage: the law solved KPL's contract disputes with Mesa, ERG, and others; preserved KPL's long-term contracts while relieving KPL of the payment obligations it had assumed as consideration for its assured supply of gas; and protected KPL's profits and rate base by discouraging conservation by KPL's many industrial customers.

The most generous assessment of this law fails to reveal that it serves any broad societal interest. In contrast to prior cases in which this Court has rejected Contract Clause challenges to the authority of public service commissions to set universally applicable rates charged by regulated utility monopolies, *e.g.*, *Fort Smith Spelter Co.* v. *Clear Creek Oil & Gas Co.*, 267 U.S. 231 (1925); *Union Dry Goods Co.* v. *Georgia Public Service Corp.*, 248 U.S. 372 (1919), this case concerns legislation that cuts with surgical precision at the contract obligations of a few; allows the benefited party to escape statutory restrictions by unilateral, voluntary agreement; and has, at best, an incidental, uneven, and minimal impact on rates paid by consumers.[47]

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[47] *Fort Smith Spelter* and *Union Dry Goods* both involved Contract Clause challenges to the rates charged by a public utility on the ground that the rates were higher than those set by private

To sustain the Kansas statute, KPL relies heavily upon § 602(a) of the NGPA, 15 U.S.C. § 3432(a), which provides that the NGPA does not preempt the power of States to "establish or enforce any maximum lawful price for the first sale of natural gas produced in [the] State." See, *e.g.*, Motion to Dismiss 1, 2, 5, 9, 10. But, even leaving aside the question whether the Kansas statute's tailored restrictions amount to "price controls" within the meaning of § 602(a), it is quite clear that § 602(a) is not an invitation for States to pass laws violative of the United States Constitution. It merely leaves with the States the power—which could have been preempted by Congress—to act, under their police powers, within the constitutional limits articulated by this Court. If the

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contracts. Yet in both instances, the utility was a state-sanctioned monopoly whose rate-making process was a public one in which the aggrieved private parties had ample opportunity to protect their interests, and the complainants were on fair notice of the possibility of state rate changes when they entered into the contracts. 267 U.S. at 232; 248 U.S. at 373-74. Equally distinguishable on similar grounds are *Cities Serv. Gas Co.* v. *Peerless Oil & Gas Co.*, 340 U.S. 179, 184 (1950) (rejecting due process attack); *Midland Realty Co.* v. *Kansas City Power & Light Co.*, 300 U.S. 109 (1937) (rejecting Contract Clause and due process challenges); *Cedar Rapids Gas Light Co.* v. *City of Cedar Rapids*, 223 U.S. 655, 667, 669 (1912) (no violation of contract); *Willcox* v. *Consolidated Gas Co.*, 212 U.S. 19, 43-44 (1909) (dismissing confiscation claim without prejudice).

Moreover, in *Arkansas Natural Gas Co.* v. *Arkansas R.R. Comm'n*, 261 U.S. 379 (1923), this Court considered a claim that a public utility commission should have fixed certain rates even though they would have contravened preexisting contracts. The Court put the question aside with but "brief consideration," stating:

> "While a State may exercise its legislative power to regulate public utilities and fix rates, notwithstanding the effect may be to modify or abrogate private contracts . . . there is, quite clearly, no principle which imposes an obligation to do so merely to relieve a contracting party from the burdens of an improvident undertaking. . . . *Indeed the exertion of legislative power solely to that end is precluded by the contract impairment clause of the Constitution.*" *Id.* at 382-83 (emphasis added).

state legislation lacks the characteristics described in *Blaisdell*, and its recent progeny, it is unconstitutional, see *New England Power Co.* v. *New Hampshire*, 50 U.S.L.W. 4223, 4225-4227 (U.S. Feb. 24, 1982),[48] and Congress could have neither the intention nor the power to change that result.[49]

The Kansas Price Protection Act is, in short, the very kind of special legislation that the Contract Clause is

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[48] In *New England Power*, this Court invalidated on Commerce Clause grounds a New Hampshire statute which empowered the state utilities commission to prohibit out-of-state exportation of electrical energy generated by water power. One of the State's arguments to sustain the law was that it was authorized by the "savings clause," § 201(b), of the Federal Power Act, 16 U.S.C. §824(b) (Supp. IV 1980), and the Supreme Court of New Hampshire agreed. 50 U.S.L.W. at 4225-26. This Court disagreed, holding that "by its plain terms, § 201(b) simply saves from preemption under Part II of the Federal Power Act such state authority as was otherwise 'lawful,'" and that laws invalid under the Commerce Clause are not "lawful" because "the Commerce Clause—independently of the Federal Power Act—restricts the ability of the States to regulate matters affecting interstate trade." *Id.* at 4226, 4227. The "nonpreemption" provision in *New England Power* is analogous to § 602(a) in this case, and this Court's analysis applies here with equal force.

[49] While the NGPA Conference Committee Report includes a sentence pertaining to a State's authority under § 602(a) to impose limitations on the operation of indefinite escalator clauses in intrastate contracts, the Conference Committee contemplated that such limitations would be part of or ancillary to a State's imposition of constitutional, generally applicable price ceilings lower than those of the NGPA. H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 125 (1978). As FERC has concluded, the conferees afforded "states under § 602(a) the authority to further limit the operation of price escalator clauses *as an adjunct* to their authority to prescribe lower maximum lawful prices for the first sale of natural gas produced within the state." 44 Fed. Reg. 16895, 16898 (March 20, 1979) (emphasis added). Under the Kansas statute, however, the selective abrogation of price escalator clauses is not "an *adjunct* to . . . [a schedule of] lower maximum lawful prices"; Kansas has chosen *not* to impose price ceilings on natural gas generally, but only to restrict certain escalator clauses.

supposed to prevent, in which the State has "adopt[ed] as its policy" the repudiation of one party's contractual obligations to another. *Blaisdell*, 290 U.S. at 439. Since there has been no showing that "this severe disruption of contractual expectations was necessary to meet an important general social problem[,] [t]he presumption favoring 'legislative judgment as to the necessity and reasonableness of a particular measure,' *United States Trust Co.*, 431 U.S. at 23, simply cannot stand in this case." *Allied Structural Steel*, 438 U.S. at 247.

2. The means employed by this statute are not necessary or reasonable to solve an important general social problem.

Assuming, *arguendo*, that the Kansas statute seeks "to safeguard the vital interests" of the people of Kansas, *Blaisdell*, 290 U.S. at 434 (quoted in *Allied Structural Steel*, 438 U.S. at 242), this Court must decide whether the legislature has adopted an appropriate, carefully conditioned means to achieve its end, without unnecessarily impairing contractual rights. "Despite the customary deference courts give to state laws directed to social and economic problems," *Allied Structural Steel*, 438 U.S. at 244, legislation modifying contract obligations must employ means that are both (a) "necessary" to serve the "important public purpose" and (b) "reasonable" in their terms and conditions. *United States Trust*, 431 U.S. at 25.[50]

(a) As was the case in *United States Trust*, "without modifying the [contract] at all, the State[] could have adopted alternative means of achieving [its] goal[]" of protecting consumers from price increases. 431 U.S. at

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[50] We understand these two requirements to be a distillation, by the Court in *United States Trust*, of the third through fifth requirements established in *Blaisdell*, each of which must be met to sustain the statute. See note 38, *supra*.

29-30; see *City of El Paso*, 379 U.S. at 516-17.[51] The KCC, after all, has authority to protect the interests of Kansas energy consumers; by denying KPL a pass-through of all or part of its increased costs, it could have achieved the goal of consumer protection. See note 44, *supra*. Indeed, the legislature could have asserted its own authority (otherwise delegated to the KCC) to prohibit all or part of the pass-through of increased costs to consumers. The legislature created a false dichotomy insofar as it assumed that it had to side with either producers or consumers in this instance. KPL carefully considered and then agreed to these indefinite escalator clauses knowing full well that rising natural gas prices were in the offing, and it therefore bears major responsibility—for which it should be held accountable—for any consequent increases in the cost of its purchased gas.

Second, in lieu of denying a pass-through of increased fuel costs, the Kansas legislature could have adopted "incremental pricing" rules similar to those Congress has mandated for interstate pipelines. NGPA §§ 201-208, 15 U.S.C. §§ 3341-3348; see 18 C.F.R. § 282.14 (1981)

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[51] Although *United States Trust* dealt with a State's impairment of its own contract obligations, its necessity test was expressly applied in *Allied Structural Steel*, where "there was no similar element of state self-interest, but the Court indicated that the customary deference would not stand when the legislation appeared to aid 'a narrow class' and there was no showing on the record that it was necessary to advance important public goals." Note, *The Supreme Court, 1977 Term*, 92 Harv. L. Rev. 57, 95 (1978) (footnotes omitted). See also *La Fortune* v. *Naval Weapons Center Fed. Credit Union*, 652 F.2d 842, 848 (9th Cir. 1981). Moreover, state courts have applied an equally stringent "necessity" standard, cautioning that state laws impairing private contract obligations must be "carefully drawn to show that the use of such power is necessary and exigent and serves a vital purpose of government.'" *Wipperfurth* v. *U-Haul Co. of W. Wis., Inc.*, 304 N.W.2d 767, 773 (Wis. 1981) (quoting *State ex rel. Bld'g Owners* v. *Adamany*, 219 N.W.2d 274, 286 (Wis. 1974)).

(States have the power to adopt incremental pricing rules for intrastate gas). Under such rules, KPL's increased costs under indefinite escalator clauses would be passed on more rapidly to "low priority" users (primarily industrial concerns) which could better absorb them and substitute more economical fuel sources. The purpose of these rules is to cushion the impact of increasing fuel costs on ordinary consumers,[52] and their promulgation would therefore go far toward achieving the purported goal of the Price Protection Act—but without impairing pre-existing contracts.

(b) The Kansas P[illegible]e Protection Act is far from a reasonable measure fo[illegible] accomplishing the legislature's stat[illegible]l goal. While it has a severe impact on legitimate contractual expectations, its limited scope and abundant exemptions insure that it could not even begin to solve the problem of rising utility costs. Although the court below found in the statute's exceptions a measure of reasonableness and tailoring, J.S. App. 20a-21a, the statute's arbitrary selectivity and under-inclusiveness merely reinforce the conclusion that it is invalid.

The most obviously arbitrary feature of this statute is its allowance of *voluntary* renegotiation of prices even in contracts otherwise covered by the statute, including

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[52] "High-priority users, including homeowners, burdened by substantial increases in delivered natural gas prices during the past several years, are temporarily insulated from further substantial price increases through incremental pricing provisions. The program has a secondary benefit; incremental pricing encourages large low-priority [industrial] users to become more efficient in their use of natural gas or to convert to more plentiful fuels." H.R. Rep. No. 95-496, 95th Cong., 1st Sess. 10-11 (1977).

An incremental pricing scheme, however, would have been at odds with KPL's interests. Incremental pricing forces cost-induced conservation among those consumers best able to curtail their demand —business and industry—and would have a depressant effect on KPL's rate base. KPL's interests favor stimulating demand as much as possible so as to increase its rate base. P. Starrett, *The Natural Gas Shortage and the Congress* 3 (1974).

the ones here at issue. J.S. App. 62a. This exemption enables KPL to exact concessions from ERG and other natural gas producers in exchange for KPL's agreement to pay the price it previously contracted for. While the court below thought this allowance of voluntary negotiations for new contract price provisions "guarantee[s] a measure of fairness," J.S. App. 21a, nothing could be more unfair than transforming KPL's contractual obligations into agreements that allow KPL to dictate unilaterally the terms by which it would honor its previous commitments.

Moreover, the statute's prohibition is unduly harsh in that it lacks the temporary character found so important in *Blaisdell*. 290 U.S. at 440, 445; see *Allied Structural Steel*, 438 U.S. at 242. The court below saw virtue in the fact that the Kansas statute expires on December 31, 1984, see J.S. App. 20a, but that fact is not relevant. In *Blaisdell*, the *impairment* was temporary because effectuation of the mortgagee's enforcement rights was merely postponed. Here, on the other hand, the statute's effect is permanent and irrevocable. ERG is required to sell its gas to KPL at a price far below market value from December 1, 1978, at least through December 31, 1984. ERG will *never* recoup these losses. The statute's life may expire at the end of 1984, but the impairment is permanent.[53]

KPL has attempted to portray the uneven contours of the Price Protection Act as reasonable by characterizing indefinite escalator clauses as against the public interest and generally undesirable. Motion to Dismiss at 5-6 & n.13, 23-24 & nn.60-62. But Kansas has never before

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[53] In addition, if the Price Protection is not invalidated, it is possible that the Kansas legislature will extend its terms beyond December 31, 1984.

prohibited or restricted the use of these clauses; KPL, a large and sophisticated public utility, freely agreed to the inclusion of such clauses in a third of its contracts;[54] and, as all parties to this appeal agree, the NGPA specifically contemplates that indefinite escalator clauses will be allowed to operate up to the § 102 ceiling. See p. 22, *supra*.[55] And, if the Kansas legislature believed that

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[54] As KPL's Executive Vice President cogently observed in testimony before the Kansas legislature in February 1979: "Producers and ourselves have never been under any type of wellhead price control. Negotiations for the price of gas have always been between a willing buyer and a willing seller with no government intervention." *Minutes, February 28 Hearing, supra* note 11 (attached statement of J.G. Williamson, Exec. Vice Pres., KPL at 1).

[55] In its attempt to demonstrate that indefinite escalator clauses are undesirable, KPL has relied on the Federal Power Commission's ("FPC") imposition of certain limitations on those clauses pursuant to a regulatory format which antedated the NGPA. In *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 782 (1968), however, this Court approved an FPC limitation proscribing the operation of indefinite escalator clauses *only* to the extent they exceeded *general* area-wide rates then set by that agency. This is the same type of prohibition found within the NGPA itself and contemplated by § 602(a). Moreover, in sustaining the constitutionality of the regulation in *Permian Basin*, the Court relied in part on the fact that parties affected by it would be offered opportunities to abandon their activities or to seek relief from the FPC rather than honor the prohibition. *Id.* at 770, 772. The Kansas Supreme Court, however, expressly construed the Price Protection Act as prohibiting contract termination by gas producers, J.S. App. 23a-24a, and there is no provision within the statute for *ad hoc* relief. Thus the ameliorative factors found to be so important in *Permian Basin* are not afforded under the Kansas statute.

Before *Permian Basin*, the FPC had proscribed the use of certain escalator clauses, but that proscription was *prospective* only, and did not abrogate existing contracts as is the case here. See Order No. 242, 27 F.P.C. 339 (1962), *currently codified at* 18 C.F.R. § 154.93 (1981); *FPC* v. *Texaco, Inc.*, 377 U.S. 33 (1964). In any event, the constitutionality of any Congressional limitation on existing contracts under its Commerce Clause powers depends on the due process clause of the Fifth Amendment and not the Contract Clause, which does not apply to the federal government. Compare this Court's analysis in *Allied Structural Steel, supra*, with *Hodel*

indefinite escalator clauses were against the public interest, it would not have excluded from the statute's reach indefinite escalator clauses associated with intrastate sales of stripper-well gas and gas from new wells and new reservoirs; nor would it have exempted all contracts entered into after April 20, 1977.[56]

C. Summary.

This is a case where the state legislature has acted "[w]ith studied indifference to the interests of the [natural gas producer] or to [its] appropriate protection." *W.B. Worthen Co.* v. *Kavanaugh*, 295 U.S. 56, 60 (1935). Just as the state legislators in *Kavanaugh* took from a mortgagee "the quality of an acceptable investment for a rational investor," *id.* at 60, those here have taken from ERG the quality of an acceptable commercial transaction for a rational entrepreneur. "So viewed [the state legislation is] seen to be an oppressive and unnecessary destruction of nearly all the incidents that give attractiveness and value" to the contracts at issue here. *Id.* at 62; see *United States Trust Co.*, 431 U.S. at 56 (Brennan, J., dissenting). It cannot be sustained.

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v. *Indiana*, 452 U.S. 314, 323-324 (1981) ("A court may invalidate legislation enacted under the Commerce Clause only if . . . there is no reasonable connection between the regulatory means selected and the asserted ends.")

[56] In *Kerr-McGee Corp.*, *supra* note 28, 673 F.2d at 327, the Tenth Circuit, while noting that the NGPA sanctioned indefinite escalator clauses, mentioned in passing that Kansas, by virtue of the Price Protection Act and the decision below, had "alter[ed] the public policy expressed in the NGPA by enacting greater restrictions on the use of indefinite price escalation clauses." The Tenth Circuit did not consider the many exemptions within the Kansas restriction of indefinite escalator clauses, nor did it address the Price Protection Act's validity.

II. UNDER THE NGPA AND THE GOVERNMENT PRICING CLAUSE OF THESE CONTRACTS, THE PRICE OF THE NATURAL GAS INVOLVED HERE ESCALATED AS OF DECEMBER 1, 1978, TO THE CEILING SET BY § 102 OF THE NGPA.

Under the government pricing clause of each of these contracts, ERG and KPL agreed that if any regulatory or governmental authority should "at any time" fix a price for any vintage of natural gas "higher than the contract price then in effect under this gas contract," the price under the contract "shall be increased to equal such regulated price." J.S. App. 66a. The price escalation automatically required by this clause takes effect as of the date of the relevant regulatory action or its effective date, whichever is later. *Id.* The Supreme Court of Kansas held, and it is now beyond dispute, that an "enactment[] such as the NGPA" constitutes regulatory action fixing natural gas prices within the intendment of the government pricing clause. See J.S. App. 14a. Since the NGPA set regulated prices higher than the contract price, the price under these contracts escalated as of December 1, 1978, to the "regulated price" authorized by the NGPA.[57]

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[57] Since the NGPA's effective date (December 1, 1978) was later than the date of its enactment (November 9, 1978), ERG was entitled to the escalated price as of December 1 according to the terms of the government pricing provision.

While ERG thus was entitled to price escalation under the government pricing clause as of December 1, 1978, it could not have had a price redetermination (under the price redetermination clause) until November 1979, because the latter clause allows redetermination only once every two years. See p. 4, *supra*. In this and certain other respects, the government pricing clause affords ERG greater rights than the price redetermination clause. If this Court should invalidate the Kansas Price Protection Act, therefore, this Court still would have to address the statutory question presented herein if ERG is to receive the full price increases to which it is entitled. If, on the other hand, this Court should sustain the constitutionality of the Kansas statute, it still would be necessary to decide the statutory question. This is because the government pricing clause

The Kansas Supreme Court recognized that under the government pricing clause, escalation based on NGPA prices would occur on December 1, 1978. J.S. App. 14a. But the court became confused when it examined § 105(b) of the NGPA, which sets price ceilings for intrastate gas (such as this) under contract on November 9, 1978. Section 105(b)(1) establishes the price ceiling for natural gas (such as this) with a November 9, 1978 "contract price" lower than the § 102 price for November 1978.[58] Under § 105(b)(1), the ceiling price in any month is either (a) the current price provided for "under the terms of the existing contract, . . . as such contract was in effect on [November 9, 1978]," or (b) the § 102 price for that month, whichever is lower.[59] The court below held that "under the terms of the government price escalator clause in these contracts, and under the applicable section of the NGPA [§ 105(b)(1)], *the November 9th*

(whose operation is barred under the Kansas Supreme Court's construction of § 105(b)(1) of the NGPA) also affords ERG greater escalation than the price redetermination clause even within the limited sphere of operation (up to the NGPA § 109 ceiling) permitted by the Price Protection Act. See note 31, *supra*.

[58] Section 105(b) contains two different pricing rules, depending on what the contract price was on November 9, 1978. If the contract price on November 9 was equal to or lower than the ceiling price set by § 102 for that date, then the maximum lawful price thereafter is governed by § 105(b)(1). If the November 9 contract price was higher than the § 102 price, then § 105(b)(2) governs. Under the contracts in question, the contract price on November 9 was $1.77 per Mcf, which was lower than the § 102 price for that date ($2.06 per MMBtu). Subsection (b)(1) of § 105 therefore governs here, and subsection (b)(2) has no application.

[59] Section 105(b)(1) sets a maximum lawful price of

> "the lower of—
>
> (A) the price under the terms of the existing contract, to which such natural gas was subject on November 9, 1978, as such contract was in effect on such date; or
>
> (B) the maximum lawful price, per million Btu's computed for such month under section 3312 of this title [§ 102] (relating to new natural gas)."

gas price (which was lower than the Section 102 price) did not escalate." J.S. App. 14a-15a (emphasis added).

The court's error is apparent. The court misconstrued § 105(b)(1) by reading its reference to "the price under the terms of the existing contract, . . . as such contract was in effect on [November 9, 1978]," to mean "the contract price on November 9, 1978." Because the contract price on November 9 was lower than the § 102 price for December 1978, the court applied the rule of § 105(b)(1) to conclude that the November 9 contract price was the maximum price for these contracts under § 105(b)(1) for December 1978 (and, by implication, for every subsequent month of the duration of the NGPA).

The Kansas Supreme Court's construction of § 105(b)(1) makes no sense. Section 105(b)(1) comes into play *if and only if* the contract price on November 9, 1978 was lower than or equal to the § 102 price for that date. By reading § 105(b)(1)'s reference to the "price under the terms of the existing contract, . . . as such contract was in effect on [November 9]" to mean the November 9 "contract price," in order to make the required comparison with the § 102 price for any month, the Kansas Supreme Court froze the § 105(b)(1) price at the level of the November 9 contract price, because the contract price on November 9 will never change and always will be lower than the constantly increasing § 102 price. See p. 6, *supra*. This reading entirely defeats Congress' purpose, specifically expressed in the Conference Committee Report, to give effect to all escalation clauses in existence on November 9, 1978, up to the § 102 price:

> "If the contract price in effect on the date of enactment is less than the new gas ceiling price, the maximum lawful price for any subsequent month is the lower of (1) the price under the terms of the existing contract in effect on the date of enactment, or (2) the new gas price. *Thus, the price under the contract may escalate through the operation of both*

> *fixed price escalator clauses and indefinite price escalator clauses in existence as of the date of enactment, but the price may not exceed the new gas price.*" H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 82 (1978) (emphasis added).

Under the Kansas court's analysis, § 105(b)(1), which was specifically written to permit escalation according to contract terms such as these, will never operate.[60]

Had Congress intended in § 105(b)(1) to focus on the November 9 contract price, it could have said so in clear terms. Indeed, this is what Congress did in § 105(b)(2). That section governs when the contract price on November 9 is higher than the § 102 price for that date, and dictates that the maximum lawful price in a given month is the higher of (a) the § 102 price for that month or (b) "the contract price on November 9, 1978," multiplied by an inflation factor for subsequent months. Congressman Dingell, a House Conferee and Chairman of the House Subcommittee responsible for the NGPA, explained: "The phrase 'the price under the terms of the . . . contract' used in section 105(b)(1) refers to the contract schedule of prices or contract mechanism for establishing prices *over time*." 124 Cong. Rec. H13117 (daily ed. Oct. 14, 1978) (emphasis in original). That

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[60] The Kansas Supreme Court's reading of § 105(b)(1) is inconsistent with the NGPA's statutory scheme in another respect. Congress meant for the NGPA ceiling prices to increase each month. See 47 Fed. Reg. 17981 (April 27, 1982). For example, in other NGPA provisions applying to intrastate gas, Congress provided that the ceiling would go up by an inflation adjustment factor each month. See NGPA §§ 105(b)(2)(B)(ii), 106(b)(1)(A)(ii) and (B)(ii), and 109(b)(1)(B), 15 U.S.C. §§ 3315(b)(2)(B)(ii), 3316(b)(1)(A)(ii) and (B)(ii), and 3319(b)(1)(B). The escalator clauses in private contracts covered by § 105(b)(1) were to serve the same purpose under that provision as the statutory escalators serve in the cited examples. Under the view taken by the court below, of course, the § 105(b)(1) ceiling—alone among the intrastate gas ceilings—is frozen for the entire life of the NGPA.

phrase "must be distinguished from the phrase 'contract price' used in section 105(b)(2). The latter is date specific, referring to the price paid under the contract for gas deliveries on date of enactment." *Id.*[61]

For these reasons, both FERC[62] and the Courts of Appeals for the Fifth and Tenth Circuits have interpreted § 105(b)(1) as we do.[63] Furthermore, the United States and FERC have urged this Court to correct the

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[61] Indeed, the term "contract price" is specifically defined in § 105(c) of the NGPA, 15 U.S.C. § 3315(c). The "contract price" for any given date is the price that actually would be paid for deliveries of natural gas on that date. Congress deliberately used different language when it wanted to describe "the contract schedule of prices or contract mechanism for establishing prices over time"; for that concept, Congress used the phrase "the price under the terms of the existing contract, to which such natural gas was subject on November 9, 1978, as such contract was in effect on such date." It is evident that Congress specified the contract to which the natural gas was subject on November 9, "as such contract was in effect on such date," so that *subsequent* modifications of contracts would not suffice to authorize higher prices under the NGPA.

[62] See 18 C.F.R. §§ 270.205(b), 271.502(a) & 271.504 (1981). The initial NGPA interim rules issued by FERC construed § 105(b)(1) ambiguously by using the terms "contract price" and "price under the terms of the existing contract" interchangeably. 43 Fed. Reg. 53270, 53344 (Nov. 15, 1978) (proposed § 271.502(a)(1)). FERC amended its interim regulations to track the statutory language, 43 Fed. Reg. 56448, 56564 (Dec. 1, 1978) (proposed § 271.502(a)(1)), in order to "allay the apprehension of those commentors who feared that fixed or indefinite price escalator clauses in contracts were abrogated by § 271.502(a)(1)." *Id.* at 56475. The final FERC regulations provided that contractual escalator provisions may operate to raise prices to the appropriate NGPA ceiling, 18 C.F.R. § 270.205(b) (1981), and expressly distinguished between "contract price" and "price under the terms of the existing contract." *Id.* § 271.504. FERC explained that the regulations, in their final form, construed § 105(b)(1) to permit escalator clauses to operate to raise the price up to the § 102 price. 44 Fed. Reg. 16895, 16904 (March 20, 1979).

[63] In reviewing FERC's regulations under the NGPA, the Court of Appeals for the Fifth Circuit agreed with FERC's construction

erroneous interpretation of the NGPA by the Kansas Supreme Court. See note 2, *supra*.

Indeed, KPL has not attempted to explain or support the Kansas Supreme Court's reading of this federal statute. Rather, it has urged this Court to view the ruling below as no more than an interpretation of the language of a particular contract. See Motion to Dismiss at 28-29 & n.14. The contention is frivolous. While the Kansas Supreme Court stated that ERG was not entitled to a price increase "because the contracts herein did not contain a sufficient escalation mechanism," J.S. App. 15a, the sole basis for the court's view as to the insufficiency of the contract escalation mechanism was its erroneous reading of the federal statute. The supposed contractual insufficiency is found in the fact that escalation is deferred until the effective date of the NGPA (December 1, 1978), such that "*the November 9th price* . . . continued until December 1, 1978, under the clear terms of the contracts." J.S. App. 14a (emphasis added). The only relevance of this conclusion, however, and the only use to which it was put by the Kansas court, was to determine the November 9, 1978 "contract price," rather than to determine—as § 105(b)(1) requires—the price, on any given date, under "the terms" of the contract as such contract was in effect on November 9, 1978. Thus, the court's conclusion as to the insufficiency of the escalation clause in these contracts was based exclusively on

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of § 105(b)(1), and described that section as providing that "the maximum lawful price is the lower of the Section 102 price or the *current* price under the existing intrastate contract (*rather than the November 9th price*)." *Pennzoil Co.* v. *FERC*, *supra*, 645 F.2d at 376 (emphasis added). "If . . . the price on November 9th was less than section 102, under section 105(b)(1) the maximum lawful price is the *current price provided for under the terms of the contract* as long as it does not exceed the section 102 price . . . ." *Id.* at 374-75 (emphasis added). The Tenth Circuit, in *Kerr-McGee Corp.* v. *Northern Utilities, Inc.*, *supra* note 28, 673 F.2d at 326, has interpreted § 105(b)(1) similarly.

its erroneous interpretation of the language of the federal statute. That erroneous interpretation should be corrected by this Court.

CONCLUSION

For the foregoing reasons, this Court should reverse the decision of the Kansas Supreme Court.

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APPENDIX

Month	Natural Gas Ceiling Prices * § 102	§ 109	Price Paid by KPL to ERG for Gas at Issue **
December 1978	$2.078	$1.630	$1.79
January 1979	2.096	1.639	1.79
February 1979	2.116	1.650	1.79
March 1979	2.136	1.661	1.79
April 1979	2.156	1.672	1.79
May 1979	2.177	1.684	1.79
June 1979	2.198	1.696	1.79
July 1979	2.220	1.708	1.79
August 1979	2.244	1.722	1.79
September 1979	2.268	1.736	1.79
October 1979	2.292	1.750	1.79
November 1979	2.314	1.762	1.79
December 1979	2.336	1.774	1.81
January 1980	2.358	1.786	1.81
February 1980	2.381	1.799	1.81
March 1980	2.404	1.812	1.81
April 1980	2.428	1.825	1.81
May 1980	2.453	1.839	1.81
June 1980	2.478	1.853	1.81
July 1980	2.504	1.867	1.81
August 1980	2.532	1.883	1.81
September 1980	2.560	1.899	1.81
October 1980	2.588	1.915	1.81
November 1980	2.614	1.929	1.81
December 1980	2.640	1.943	1.83
January 1981	2.667	1.957	1.83
February 1981	2.698	1.975	1.83
March 1981	2.729	1.993	1.83
April 1981	2.761	2.011	1.83
May 1981	2.787	2.024	1.83
June 1981	2.813	2.037	1.83

[Continued on page 2a]

* 47 Fed. Reg. 17981, 17982 (April 27, 1982), *to be codified at* 18 C.F.R. § 271.101(a) (excerpt from Table I).

** This price represents the base price to which minor adjustments are made (upward or downward) depending upon the heating value of the gas. See J.S. App. 66a.

Month	Natural Gas Ceiling Prices § 102	§ 109	Price Paid by KPL to ERG for Gas at Issue
July 1981	2.840	2.050	1.83
August 1981	2.863	2.060	1.83
September 1981	2.886	2.070	1.83
October 1981	2.909	2.080	1.83
November 1981	2.940	2.096	1.83
December 1981	2.971	2.112	2.096
January 1982	3.003	2.128	2.096
February 1982	3.033	2.143	2.096
March 1982	3.063	2.158	2.096
April 1982	3.093	2.173	2.096
May 1982	3.112	2.180	2.096
June 1982	3.132	2.187	2.096
July 1982	3.152	2.194	2.096

Appellee's Brief

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No. 81-1370

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

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QUESTIONS PRESENTED

I. Whether state imposition of price controls in the Kansas Natural Gas Price Protection Act, as authorized by the Natural Gas Policy Act of 1978, violates the Contract Clause of the United States Constitution when the Act furthers the legitimate state goal of intrastate gas price regulation, and when the Act does not benefit Kansas utilities whose wholesale gas cost increases are, under Kansas administrative orders, directly borne by Kansas consumers.

II. Whether Congressional enactment of the Natural Gas Policy Act of 1978 "fixed a higher price," within the meaning of Appellant ERG's contracts, when the NGPA imposed, as the ceiling for ERG's natural gas, the "terms of ERG's contracts."

PARTIES BELOW

The only parties to this proceeding in the Court below are those indicated by the caption of this brief. Appellee The Kansas Power and Light Company has no parent corporation, subsidiaries or affiliates.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1370

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

BRIEF FOR APPELLEE

STATEMENT OF THE CASE

This appeal challenges the constitutionality of wellhead natural gas price controls, which the State of Kansas enacted as the intrastate component of, and pursuant to express authorization in, the Natural Gas Policy Act of 1978 ("NGPA").[1] Requested by the Kansas Governor, and enacted by overwhelming majorities in both state legislative bodies, the Kansas Natural Gas Price Protection Act ("Price Protection Act" or the "Act")[2] imposes, on indefinite price escalations for Kansas intrastate gas, price ceilings equal to those imposed by the NGPA at the interstate level. This is one in a series of cases filed in Kansas by producers who seek for their old intrastate gas the maximum NGPA new gas incentive

[1] 15 U.S.C. § 3301, *et seq.* (Supp. IV 1980). Citations herein are to the Jurisdictional Statement ("J.S."), the Appendix filed therewith ("J.S.App."), the Joint Appendix ("App."), and the Record on Appeal ("R.Vol.") by document title.

[2] Kan. Stat. Ann. §§ 55-1401, *et seq.* (Supp. 1980).

price, which Congress established as an intrastate ceiling expressly subject to state authority to impose more stringent controls.

Energy Reserves Group, Inc. ("ERG") seeks in this litigation to circumvent this Court's traditional approval of state price controls on natural gas. Citing the "plain terms of the contracts" and "the law governing public utilities" in 1934,[3] ERG contends that the Kansas Act was special legislation intended to serve the "great stake" of The Kansas Power and Light Company ("KPL") in avoiding the "probability" of absorbing increased gas costs.[4] As two state agencies informed the Legislature,[5] however, regulated utilities in Kansas had no financial self-interest in legislation that affected wellhead natural gas costs. Two years *after* execution of these contracts, Kansas in 1977 administratively adopted a "purchased gas adjustment clause," which directed the immediate and automatic pass-through to consumers of all increased gas costs incurred by regulated utilities.[6] After the NGPA reserved to the states responsibility for intrastate gas

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[3] Appt's Reply to Motion to Dismiss, 1 (citing *State Corp. Comm'n v. Wichita Gas Co.*, 290 U.S. 561 (1934)); Appt's Br. 31-32.

[4] Appt's Br. 16, 31. ERG understandably made no factual claims in the record below to support this contention. This case was submitted to the trial court on cross-motions for summary judgment on ten stipulated facts. J.S.App. 25a-26a. ERG assured the Court that these constituted the only material facts necessary for resolution of the constitutional question. Plaintiff's Memorandum In Opposition to Motion for Leave to File, Filed Mar. 5, 1980, at 4, 6, R.Vol. III at 90, 92; Transcript of Hearings Held On Mar. 6, 1980, at 87, R.Vol. IV at 87.

[5] Kansas Legislative Research Dep't, *Minutes, Hearings Before the Special Comm. on Energy and Natural Resources* (May 9-11, 1979) (statements of R. Loux, J. King, Attachments 7, 8) (hereinafter "Minutes, May Hearings"). *See also* App. 8.

[6] Kansas Corp. Comm'n, *In re General Investigation Upon the Commission's Own Motion To Establish General Policies With Regard to Purchased Natural Gas*, Docket No. 106,850-U (April 19, 1977) (hereinafter "PGA Order").

pricing policy under new market conditions, the Kansas Act represented a legitimate effort to create a responsible state pricing policy consistent with the philosophy of the NGPA.

A. The Contracts

ERG is an oil and natural gas producer in the Spivey-Grabs natural gas field in southern Kansas. KPL is a public utility regulated by the provisions of Kan. Stat. Ann. §§ 66-104 et seq. (1980). KPL holds appropriate certificates to transact business as a gas utility in the State of Kansas. ERG and twenty-seven other natural gas producers in the Spivey-Grabs field jointly negotiated with KPL a standard contract, which offered this gas to KPL on the terms of a single contract that KPL could execute with each individual producer.[7] In 1975, KPL executed approximately 75 virtually identical contracts with these twenty-eight producers to obtain gas production from approximately 125 gas wells in the field.[8] KPL executed two of these contracts with ERG.

ERG's initial contract price in 1975 was $1.50 per Mcf. J.S.App. 66a. Although ERG claims that it made a "sacrifice" to accept this initial "low price," Appt's Br. 3-4, this price then exceeded the average price for new intrastate contracts executed by utilities in the region.[9]

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[7] Kansas Corp. Comm'n, *In Re Petition of KPL for Implementation and Enforcement of the Provisions of the Kansas Natural Gas Price Protection Act*, Docket No. 126,236-U, Transcript of Hearing on March 24, 1981, at 53-54 (Testimony of G. Benignus).

[8] *Id.* Major producers in the field include Mobil Oil, Atlantic-Richfield, Phillips Petroleum, Sun Oil, and Superior Oil.

[9] The average price paid in 1975 by utilities in Texas, Louisiana, Oklahoma and Kansas was $0.83 per Mcf. The average price for new intrastate contracts executed in 1975 in these states was $1.29 per Mcf. Staff of Subcomm. on Energy, Joint Economic Comm. of Congress, 95th Cong., 1st Sess., *The Economics of the Natural Gas Controversy*, 18 (Comm. Print 1977) (hereinafter "Economics of the Gas Controversy").

The contracts also contained a single, fixed price escalation clause that provided, not more than once each year, a price increase of two cents per Mcf. J.S.App. 66a.

ERG's contracts contain two "indefinite price escalator clauses." [10] ERG's "government pricing" clause triggers an increase equal to a higher price for natural gas in Kansas "fixed" by a governmental authority. J.S.App. 66a. The "price redetermination" clause permits, on a designated date once every two years, a price adjustment up to the weighted average price under three other contracts for the sale of gas in Kansas. J.S.App. 67a. ERG's contracts specifically provide that all of the price terms, including the indefinite price escalator clauses, are subject to "all relevant present and future state and federal laws." J.S. App. 69a.

One year after the execution of these contracts, the Kansas Corporation Commission ("KCC") commissioned a study of the feasibility of adopting, for regulated utilities in Kansas, a "purchased gas adjustment" ("PGA") clause, which would authorize the automatic pass-through of wholesale gas cost increases to consumers. The PGA clause is a common feature of state utility regulation in most jurisdictions and reduces an unmanageable burden of rate review hearings and rate adjustments when fuel costs are rapidly rising.[11]

The KCC adopted a standard pass-through clause for gas utilities on April 19, 1977, and on June 9, 1978,

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[10] "Indefinite escalation clauses 'cause price increases . . . to occur without reference to the circumstances or economics of the particular operation, but solely because of what happens under another contract.' . . ." *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 782-83 (1968).

[11] The PGA also reduces administrative expense and efficiency losses generated by long delays in the rate review process. PGA Order, *supra* note 6, at 8-14. By 1974, PGA clauses had been employed in at least 36 states and the District of Columbia. Fowler, *Purchased Gas Adjustment Clauses: An Adjuster's Viewpoint*, 6 St. Mary L.Rev. 567, 570 n.16 (1974).

specifically gave KPL authority to implement the designated PGA clause.[12] As of that date, KPL had authority, on written notice to the KCC, to pass-through to consumers all gas cost increases due its producers.[13] Gas cost changes thus could not, as ERG speciously argues, alter the utility's earnings, nor by definition could these costs affect the utility's rate base or rate of return.

B. Enactment of the NGPA

ERG argues that the NGPA embraces "deregulation . . . as ultimately in the public interest," and establishes ceilings for old intrastate gas "at or above the § 102 level," intending that this new gas incentive price apply to ERG's old intrastate gas. Appt's Br. 24 n.32, 29. ERG misconstrues the NGPA. The NGPA constitutes a new federal policy of higher prices only for certain categories of natural gas where increased production and supplies might result. The NGPA, through application of the § 105 ceiling, actually maintains the price for most Kansas intrastate old gas—gas not subject to indefinite escalation clauses—substantially *below* the incentive new gas price claimed by ERG. The NGPA is premised on the idea that higher prices for old gas, where production would not be stimulated, are "unfair" and "unrelated to any economic contributions of producers." [14]

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[12] PGA Order, *supra* note 6; Kansas Corp. Comm'n, *In re Application of KPL for Permission to Add "PGA" Clauses To Gas Rate Schedules*, Docket No. 114,772-U (June 9, 1978).

[13] *See, e.g., Midwest Gas Users' Ass'n v. State Corp. Comm'n*, 5 Kan.App.2d 673, 623 P.2d 924 (1981) ("increased cost of gas to Gas Service was not involved in the rate increase because such is automatically passed-through to consumers by means of the 'purchased gas adjustment' ").

[14] *Proposed National Energy Plan, Hearings Before the Subcomm. on Oversight and Investigations of the House Comm. on Interstate and Foreign Commerce*, 95th Cong., 1st Sess. 6 (1977) (statement of J. Schlesinger, Assistant to the President) (hereinafter "Hearings on Proposed Energy Plan").

The NGPA is the outgrowth of President Carter's National Energy Plan,[15] announced on April 20, 1977. The NGPA followed thirty years of Congressional debate on natural gas pricing.[16] Legislative action on the NGPA was prompted both by severe gas shortages in the interstate market and by a five-year period of dramatic oil price increases that generated corresponding increases in the price of virtually all other energy resources, including natural gas.[17]

Initial regulation of natural gas prices had been premised on the lack of competitive market conditions in the domestic natural gas industry.[18] Throughout consideration of the NGPA, Congress debated whether those market problems continued to exist.[19] Congress acknowledged,

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[15] Executive Office of the President, Energy Policy and Planning, *The National Energy Plan* (1977).

[16] See 124 Cong. Rec. S16262 (daily ed. Sept. 27, 1978) (statement of Sen. Glenn); 124 Cong. Rec. H13114, H13424 (daily ed. Oct. 14, 1978) (statements of Reps. Dingell and Woolf).

[17] *See Hearings on Proposed Energy Plan, supra* note 14, at 18 (1977) (statement of J. Schlesinger); *Economics of the Gas Controversy, supra* note 9, at 39, 59; *Natural Gas Pricing Proposals of President Carter's Energy Program, Hearings on S.256 and S.1469 Before the Senate Comm. on Energy and Natural Resources*, 95th Cong., 1st Sess. 150 (1977) (statement of E. Berlin) (hereinafter "Hearings on S.256"); *Public Impact of Natural Gas Price Deregulation, Hearings on S.2104 Before the Subcomm. on Antitrust and Monopoly of the Senate Comm. on the Judiciary*, 95th Cong., 1st Sess. 27-28 (1977) (statement of R. Nader) (hereinafter "Hearings on Deregulation"). *See Implementation of Title I of the Natural Gas Policy Act of 1978, Hearings Before the Senate Comm. on Energy and Natural Resources*, 97th Cong., 1st Sess. 110 (1981) (Statement of Dr. Cicchetti) (hereinafter "Hearings on Implementation of Title I").

[18] Comment, *For Gas, Congress Spells Relief N-G-P-A: An Analysis of the Natural Gas Policy Act of 1978*, 40 U.Pitt.L.Rev. 429, 451-458 (1979); MacAvoy & Pindyck, *The Economics of the Natural Gas Shortage* 31 (1975).

[19] Congress recognized that "fundamental structural imperfections existed in the natural gas market and they required complex,

however, that artificially high oil prices generated by OPEC cartel pricing agreements constituted a new and compelling reason to implement price controls on other energy resources whose prices were otherwise dictated by OPEC agreements.[20]

Prior to enactment of the NGPA, massive energy price increases had fueled inflation, generated additional unemployment, and contributed substantially to the economic recessions experienced since 1974.[21] With OPEC oil prices costing industrial countries $150 billion per

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careful regulation." *Hearings on Implementation of Title I, supra* note 17, at 129-30, 133, 318 (statements of Dr. Cooper, A. Verrips); *Hearings on Proposed Energy Plan, supra* note 14, at 21 (statement of J. Schlesinger); National Ass'n of Regulatory Utility Commissioners, *Survey of Action by State Regulatory Agencies and Intrastate Natural Gas Distributors to Meet Natural Gas Shortages* 4 (1974) ("in the natural gas industry . . . the conditions necessary for competition cannot be met").

[20] "Whether or not regulation was useful before 1973, the rise of OPEC placed the matter in an entirely new light. Whether the domestic gas industry is competitive or not is no longer relevant, because all uncontrolled energy prices are under the dominant influence of the OPEC cartel. Until energy supplies are forthcoming in sufficient quantity from non-OPEC sources, competitive prices will not exist. The question is simply whether the United States Government or a combination of foreign governments should set prices for domestic energy."

Economics of the Gas Controversy, supra note 9, at 12, 76.

[21] Energy price increases cost the United States economy in 1973-75 an estimated $58 billion and generated one-half of the total national inflation experienced in those years. *Economics of the Gas Controversy, supra* note 9, at iv, 59-61. An additional 150% oil price increase between 1979 and 1980 contributed more than ten percentage points to the inflation rate in 1980 and significantly reduced economic output. *See Cost to Consumers of Deregulation of Crude Oil, Hearings Before the Subcomm. on Oversight and Investigations of the House Comm. on Interstate and Foreign Commerce*, 96th Cong., 2d Sess. 2 (1980); *United States International Trade Strategy, Hearings Before the Subcomm. on International Trade of the Senate Comm. on Finance*, 96th Cong., 2d Sess. 214 (1980) (statement of R. Kubarych).

year more for oil than would be paid in competitive oil markets, and with those prices depressing standards of living annually by $50 to $100 billion,[22] Congress confronted a difficult dilemma in natural gas pricing. Comparable higher prices for natural gas were needed to stimulate exploration for, and production of, new gas resources to replace diminishing supplies.[23] Allowing prices to reach market-clearing levels with OPEC oil prices would, however, impose on American consumers "cartel-induced energy prices" and transfer tens of billions of dollars from consumers to producers, generating teriffic "windfall profits," with potentially marginal supply responses.[24]

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[22] Congressional Budget Office, *The Effect of OPEC Oil Pricing on Output, Prices and Exchange Rates in the United States and Other Industrialized Countries*, xix (February, 1981). Application of OPEC prices to domestic oil, in the absence of regulation, currently transfers more than $50 billion per year from American consumers to producers. *1981 Economic Report of the President, Hearings before the Joint Economic Comm. of Congress*, 97th Cong., 1st Sess. 230 (1981).

[23] *Economics of the Natural Gas Controversy, supra* note 9, at 12. Congress expressed some "real questions" whether this reduction in reported supply was created by producers who, in anticipation of future higher prices, artificially suppressed both production and reports of estimated recoverable reserves. "Gas left in the ground is perceived as a better investment than cash in the bank." *Id.* at 2, 23, 42-43. *See* 124 Cong. Rec. 29387 (1978) (statement of Sen. Metzenbaum); 124 Cong. Rec. S14885 (daily ed. Sept. 11, 1978) (statement of Sen. Proxmire).

[24] *Economics of The Gas Controversy, supra* note 9, at 39, 44, 87; *Hearings on S.256, supra* note 17, at 46 (statement of J. O'Leary). *See Hearings on Deregulation, supra* note 17, at 3, 27-28 (statements of Sen. Kennedy, R. Nader).

Congress estimated that the NGPA would transfer between $20 billion and $55 billon from consumers to natural gas producers between 1979 and 1984, based on expectations of 5% or 6% inflation and a $17 per barrel crude oil price. *See* 124 Cong. Rec. S16237 (daily ed. Sept. 27, 1978) (statement of Sen. Metzenbaum); 124 Cong. Rec. H13420 (daily ed. Oct. 14, 1978) (statement Rep. Harris). Actual current prices under the NGPA are 10% to 13%

Two divergent approaches to the natural gas problem emerged from Congress. To protect consumers and provide "fair and equitable producer revenues," the House bill proposed a system of nationwide price controls that extended federal regulation to the intrastate market.[25] To increase supplies, the bill provided incentive prices for "new gas," but did not permit deregulation. The Senate bill provided phased deregulation of new gas prices in the interstate market,[26] but did not extend controls to intrastate natural gas.

Debates in both houses reflected great Congressional concern for the economic impact of indefinite price escalator clauses in existing gas contracts. Without reference to market conditions or economic factors, the clauses could escalate prices for old gas up to any incentive gas price that Congress might provide. "Unless measures [were] specifically mandated to proscribe this," these clauses would subject the economy "to unnecessary inflationary drag." [27]

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higher than most projections in 1978. *Compare* Oil & Gas Journal, at 36, (May 29, 1978) *and* Staff of Subcomm. on Energy and Power of the House Comm. on Interstate and Foreign Commerce, 95th Cong., 2d Sess., *Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978* 3 (Comm. Print 1978) (hereinafter "Economic Analysis of the NGPA"), *with* 47 Fed. Reg. 32935 (July 30, 1982) (to be codified in 18 C.F.R. § 271.101).

State governors agreed that even limited allowance of an OPEC-based incentive price for new gas would, although desirable to increase gas supplies, generate "excessive profits" for the industry. National Governors' Conference, *Policy Position on Natural Gas 1976-77*, in *Hearings on S.256*, *supra* note 17, at 146.

[25] H.R. 8444, Section 401(b)(1), 95th Cong., 1st Sess. (1977). The bill passed the House on August 5, 1977. 123 Cong. Rec. 27187, 27244-45 (1977).

[26] S.2104, 95th Cong., 1st Sess. §§ 24(a)(5), 24(b)(2) (1977). The Senate passed the bill on October 4, 1977. 123 Cong. Rec. 32308 (1977).

[27] *Economics of the Gas Controversy*, *supra* note 9, at 3, 69, 85.

Intrastate markets, where no prior federal regulation had restrained use of these clauses, were most vulnerable to these adverse effects. Congress recognized the need to protect consumers of intrastate gas, either by applying nationwide ceilings or by "freezing all intrastate gas prices in one manner or another." [28] Any proposed price increases for new gas would need to include, as "an important step in holding down old gas prices," [29] language restricting the operation of escalator clauses. These restrictions were acknowledged as "especially important to intrastate markets." [30]

After months of negotiations, the Conference Committee reached a draft Agreement in Principle detailing proposed legislation with elements of both House and Senate bills. By a one vote margin, House Conferees adopted the agreement only after amendment acknowledging that states retained "authority to limit or prohibit" indefinite price escalator clauses.[31] The legislation was released on August 16, 1978, together with a Conference Report reflecting the terms of the Agreement in Principle.[32]

As enacted, the NGPA addresses three major goals: allowance of high, incentive prices for certain gas cate-

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[28] *Id.* at 87 (noting New Mexico legislation restricting intrastate gas prices).

[29] *Id.* at 85.

[30] *Id.* Even proponents of deregulation acknowledged that indefinite price escalator clauses in intrastate contracts posed a problem that should be addressed by Congress or by state regulatory agencies. *Hearings on S.256, supra* note 17, at 119, 127, 486 (1977) (statements of Sens. Bentsen & Jackson, Gov. Briscoe).

[31] Staff of House Comm. on Interstate and Foreign Commerce and Senate Comm. on Energy and Natural Resources, 95th Cong., 2d Sess., *Natural Gas Pricing Agreement Adopted by the Conferees on H.R. 5289* 19 (Comm. Print 1978). The agreement already contained language in a separate paragraph providing that states retained the right to prescribe price ceilings for intrastate gas lower than the ceilings under the Conference Agreement. *Id.* at 18.

[32] S. Rep. No. 1126, 95th Cong., 2d Sess. (1978).

gories to stimulate new production, elimination of price disparities in interstate and intrastate markets to give interstate pipelines access to new gas sources, and the achievement of these goals "with the minimum impact on the overall rate of inflation."[33] The NGPA thus extends regulation to intrastate gas and gradually introduces higher prices for new production and for continued production from low volume sources. Congress expressly found, however, that deregulation of old gas prices would have "little impact on production," but would seriously stimulate inflation and unemployment.[34] The NGPA thus indefinitely continues, as a means of consumer protection, the regulation of old natural gas prices.

This philosophy of incentive prices for additional production permeates the NGPA, which establishes, for different gas categories, a series of escalating price ceilings that limit contractual price increases for that gas. NGPA §§ 102 and 103 establish high ceilings for new gas and new gas production from known reservoirs. The NGPA removes these ceiling restrictions in 1985. NGPA § 108 provides the highest NGPA price for gas from stripper wells to encourage continued production from these low volume sources. These incentive price ceilings are equally available for interstate or intrastate gas. Deregulated prices are offered for high-cost gas qualified under § 107.[35]

For old interstate gas flowing in 1978, NGPA § 104 freezes, in real dollar terms, the various April 20, 1977,

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[33] Congressional Budget Office, Natural Resources and Commerce Division, *The Natural Gas Compromise* 2 (Aug. 2, 1978); *Economic Analysis of the NGPA*, *supra* note 24, at 2; 124 Cong. Rec. S14844-45 (daily ed. Sept. 8, 1978) (statement of Sen. Muskie); 124 Cong. Rec. S14869 (daily ed. Sept. 11, 1978) (statement of Sen. Jackson); 124 Cong. Rec. S14947 (Sept. 12, 1978) (statement of Sen. Domenici); 124 Cong. Rec. S16258 (daily ed. Sept. 27, 1978) (statement of Sen. Muskie).

[34] *Economic Analysis of the NGPA*, *supra* note 24, at 12, 13.

[35] 15 U.S.C. §§ 3312 to 3318, 3331 (Supp. IV 1980).

cost-based rates promulgated by the Federal Energy Regulatory Commission ("FERC").[36] NGPA § 109 controls other categories of old gas and establishes a ceiling equal to the highest ceiling in § 104 for old interstate gas under contract. These gas categories are not deregulated under the NGPA.

The NGPA does not grant a seller a federal right to any of these ceiling prices. "In no case may a seller receive a higher price than his contract permits."[37] New gas may thus escalate to the § 102 new gas price, for example, or stripper gas to the § 108 price, only if that gas qualifies under that NGPA category, and only "provided that the contract has a sufficient escalation mechanism"[38] to authorize that price.

Old intrastate gas not qualified for an incentive price is controlled by NGPA § 105.[39] Although other NGPA ceilings establish a specific ceiling price, § 105 establishes as the relevant ceiling the *lower* of the § 102 new gas price and the "price under the terms of the existing contract . . . in effect on [November 9, 1978]." J.S.App. 57a. Section 105 thus freezes "the terms of the contract" as they existed on the date of NGPA enactment.[40] Old intrastate gas under a contract without indefinite es-

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[36] 15 U.S.C. § 3314 (Supp. IV 1980); 47 Fed. Reg. 32935 (July 30, 1982) (to be codified in 18 C.F.R. § 271.101). *See* 124 Cong. Rec. H13117, H13129 (daily ed. Oct. 14, 1978) (statement of Reps. Dingell & Stockman); 124 Cong. Rec. 29109 (1978) (statement of Sen. Jackson).

[37] S. Rep. No. 1126, 95th Cong., 2d Sess. 74 (1978).

[38] *Pennzoil Co. v. FERC*, 645 F.2d 360, 375 (5th Cir. 1981), *cert. denied*, 50 U.S.L.W. 3547 (Jan. 11, 1982).

[39] 15 U.S.C. § 3315 (Supp. IV 1980).

[40] Section 105 also freezes, in real dollar terms, the price for old intrastate gas with prices above the NGPA § 102 price on the date of NGPA enactment. Price increases are allowed only for inflation until the § 102 price, which escalates 4% per year above inflation, exceeds that contract price. 15 U.S.C. § 3315(b)(2) (Supp. IV 1980).

calation provisions is frozen at that lower established price, plus any fixed escalations. Because § 105 limits the price under both the existing and any "successor" contract, "the producer loses the right to renegotiate later for a better price." [41]

Despite ERG's suggestion that this "old gas—new gas" analysis represents a "false distinction", [42] Congress employed this distinction to differentiate between gas that is supply responsive to higher prices, and therefore warrants incentive prices, and gas that is not. Senators acknowledged that, under the NGPA, the "price of previously discovered gas [would] be kept in proportion to the costs of producing it," and that "it would be a silly political idea to deregulate old gas." [43] "Consumers should continue to be protected by regulations which prevent the price of old, inexpensive gas from rising to the price of new, hard-to-find gas." [44]

Although the NGPA permits the operation of existing intrastate escalator clauses, Congress recognized that not every clause would necessarily adopt a new gas price. While new intrastate gas would qualify for the new gas incentive price, "[intrastate] gas not considered 'new' would get a lower price." [45] In discussing § 105, the Conferees addressed "government pricing" type clauses that

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[41] 124 Cong. Rec. S14880 (daily ed. Sept. 11, 1978) (statement of Sen. Hansen). "Successor contracts" are limited by the price term ceilings of the original contract. After intrastate contracts terminate according to their terms, subsequent contracts are deemed "rollover" contracts and are subject to upward adjustment under § 106. 15 U.S.C. § 3316 (Supp. IV 1980).

[42] Appt's Reply to Motion to Dismiss, 8.

[43] 124 Cong. Rec. S14949, S14967 (daily ed. Sept. 12, 1978) (statement of Sens. Hollings & Hart).

[44] 124 Cong. Rec. S14967 (daily ed. Sept. 12, 1978) (statement of Sen. Hart).

[45] 124 Cong. Rec. S14880 (daily ed. Sept. 11, 1978) (statement of Sen. Hansen).

adopt *higher* rates established by a governmental authority.[46] By establishing a § 105 ceiling equal to the "terms of the contract,"

> The conferees [did] not intend that mere establishment of the ceiling prices under this Act shall trigger indefinite price escalator clauses in existing intrastate contracts.[47]

The NGPA acknowledged that NGPA prices in the marketplace may trigger intrastate escalator clauses that refer to prices under other contracts.[48] Thus, "most favored nation" and price redetermination clauses, which adjust prices according to prices paid under other contracts, would operate under the NGPA.[49] Acknowledging the problem that these escalator clauses create for intrastate markets, however, the Conferees specifically "recognized the right of States to prescribe more stringent limitations" on the operation of these clauses than those prescribed by the NGPA.[50]

C. Enactment of the Price Protection Act

In its first session after enactment of the NGPA, the Kansas Legislature overwhelmingly enacted the Price

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[46] H.R. Rep. No. 1752, 95th Cong., 2d Sess. 83, *reprinted in* [1978] U.S. Code Cong. & Ad. News 9041.

[47] *Id.*

[48] "Once natural gas is sold pursuant to the ceiling prices under this Act, such clauses would be activated as limited by this Section." *Id.*

[49] "Gas purchases by others at that [§ 102] price will trigger price redetermination clauses." 124 Cong. Rec. 29652 (1978) (statement of Sen. Bartlett) ("favored nation clauses" also would be triggered); 124 Cong. Rec. S14972 (daily ed. Sept. 12, 1978) (statement of Sen. Wallop) ("most favored nation" clauses may operate). *But see* 124 Cong. Rec. S14967 (daily ed. Sept. 12, 1978) (statement of Sen. Hart) (escalation for old gas possible to new gas price only "as contracts expire").

[50] H.R. Rep. No. 1752, *supra* note 46, at 83.

Protection Act to implement the policy of state price controls embraced within the NGPA system for regulation of intrastate gas prices. The Act represented well-foreseen state restrictions that ERG and other producers specifically here seek to circumvent.[51]

Among the largest natural gas producing states in the country, Kansas has, since the beginning of the century, regulated virtually every aspect of intrastate natural gas production.[52] "For more than 70 years" Kansas has held that "the production, transportation, distribution and sale of natural gas . . . is a business of a public nature and subject to the regulation and control of the state."[53] By 1950, the KCC already possessed and had exercised the authority to fix prices of natural gas at the wellhead,[54] and Kansas was regarded as "one of the

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[51] Although ERG here argues that the Act was a "totally unanticipated change," Appt's Br. 30, ERG argued below that "the parties were aware of the potential for continuing changes in the area of regulation and even foresaw the potential of regulation of the intrastate sale of natural gas." Brief of Appellant ERG at 17, *Energy Reserves Group v. The Kansas Power and Light Company*, No. 80-52677-AS. Moreover, the escalator clauses specifically anticipate future state regulations. J.S.App. 66a, 70a ("Kansas regulatory or governmental authority" may "fix a price" for gas in Kansas; contracts are subject to "future state laws").

[52] *See* Kan. Rev. Stat. Ann. 1923 ch. 55 at 781; 1935 ch. 55 at 1174, 1188. In the first half of this century, Kansas was ranked third among the states for most natural gas reserves. Hardwicke, *Some Consequences of Fears by Independent Producers of Gas of Federal Regulation*, 19 Law & Contemp. Prob. 342, 350-51 (1954). Kansas is presently the fifth largest gas producing state in the country. Department of Energy, Energy Information Administration, *Energy Data Report* (March 4, 1982).

[53] *Cities Serv. Gas. Co. v. State Corp. Comm'n*, 222 Kan. 598, 567 P.2d 1343, 1352 (1977).

[54] *Kansas-Nebraska Natural Gas Co. v. State Corp. Comm'n*, 169 Kan. 722, 222 P.2d 704 (1950). Because Kansas wellhead price controls extended to interstate gas, they were held unconstitutional by this Court. *Cities Serv. Gas Co. v. State Corp. Comm'n*, 180 Kan. 454, 304 P.2d 528 (1957), *rev'd*, 355 U.S. 391 (1958).

articulate and forthright proponents of state regulatory powers" in the field of natural gas regulation.[55]

In November 1978, after the NGPA reserved to the states responsibility for intrastate pricing policy, Kansas elected a new governor who had campaigned on a promise of restraining utility price increases. On January 23, 1979, in his first address to the State Legislature, Governor Carlin emphasized the need for legislative action in the field of energy, noting the "mistaken belief that unguided private enterprise will be responsive to the larger public interest." [56] On February 6, 1979, S.B.252 was introduced in the Kansas Senate and proposed a freeze on the operation of indefinite price escalator clauses in intrastate gas contracts. The Kansas Senate immediately referred S.B.252 to committee and scheduled hearings on the bill for February 21, 1979.[57] Under its PGA clause, KPL at that time already had authority to pass through to consumers the increased costs that S.B.252 addressed.

When producers in Kansas saw the potential for implementation of the intrastate price controls envisioned by the NGPA, Mesa Petroleum Co. on February 15, 1979, declared, and on February 16 filed suit to enforce, termination of three large gas supply contracts with KPL based upon KPL's refusal to pay for Mesa's old gas the maximum NGPA § 102 new gas price. Mesa's notice of termination was several weeks premature under contract pro-

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[55] Note, 26 Notre Dame L. 561, 567 (1951).

[56] Office of the Governor of the State of Kansas, *Governor's Legislative Message and Budget Report* 11 ((Jan. 23, 1979).

[57] S.B. 252, Kansas Legislative Information System, *1979 Senate and House Actions Report* S45 (May 14, 1979). The KCC was the principal proponent of the legislation and testified in favor of the bill. KPL submitted a short statement in favor of the bill. Two oil companies testified against the bill. Kansas Legislative Research Dep't, *Minutes, Hearings Before the Senate Comm. on Energy and Natural Resources* (February 28, 1979).

visions,[58] and Mesa claimed, based upon enactment of NGPA ceiling prices, contractual price increases then forbidden by interim federal regulations.[59]

While S.B. 252 was still pending in the Legislature, the less restrictive Price Protection Act was introduced as H.B. 2680 in the Kansas House.[60] Governor Carlin became "the bill's principal cheerleader." [61] The Governor urged the Legislature to take positive action on the bill and threatened to call the Legislature into a special ses-

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[58] Mesa's contracts provided that termination could occur no earlier than 95 days after the price increase allegedly occurred on December 1, 1978, and thus was not proper until March, 1979.

[59] 18 C.F.R. § 270.205 (Historical Comment, Dec. 1, 1978), 43 Fed. Reg. 56448, 56463 (Dec. 1, 1978), *vacated*, FERC Order No. 23, 44 Fed. Reg. 16904 (March 20, 1979). The regulation prohibited price increases triggered by NGPA establishment of higher prices, but permitted those triggered by payment of higher prices. ERG notified KPL on December 27, 1978, that it would claim a price increase based on payment of higher prices and would "notify [KPL] of the effective date of the price increase." Exhibit 3 to Plaintiff's Memorandum Filed February 4, 1980, R.Vol. II at 90 et seq. *See also Minutes, May Hearings, supra* note 5 (statement of J. McCoy, Attachment 20) (escalations not claimed under interim regulations).

[60] Kansas Legislative Information System, *1979 Senate and House Actions Report* H98 (May 14, 1979). Although ERG implies, without authority, that introduction of the bill during a "special veto session" was unusual, the bill was one of 40 bills and 27 resolutions then introduced. Seventeen of these were enacted. *Id.* at S80-82, H98-101. In the last five legislative sessions, 139 bills and 84 separate resolutions were introduced in the late legislative session. Of these, 84 bills were enacted. *See* Kansas Legislative Information System, *1982 Senate and House Actions Report* S112-123, H139-156 (May 17, 1982); *1981 Senate and House Actions Report* S82-94, H93-106 (May 21, 1981); *1980 Senate and House Actions Report* S103-115, H144-161 (May 20, 1980); *1978 Senate and House Actions Report* S125-141, H162-182 (May 10, 1978).

[61] Kansas City Times, May 9, 1979, at 1. *See* Topeka Capitol Journal, May 18, 1982, at 1. ERG relies on newspaper articles to distort KPL's support for the Act, Appt's Reply to Motion to Dismiss, 2 n.1, even though these papers editorially endorsed the Act as beneficial to the state. Wichita Eagle, May 9, 1979, at 26.

sion on May 15, 1970, if it did not.[62] Pursuant to the Governor's request, a Special Joint Committee conducted three days of hearings on the bill.

Initial testimony in favor of the bill came from two state agencies. The KCC Chairman informed the Legislature of the 1977 adoption of the PGA clause and stated that eight principal utilities, and one cooperative of numerous rural utilities, purchased natural gas that would be subject to the bill. The Chairman specifically informed the Legislature that, "under the present fuel adjustment clause, the utilities cannot benefit economically by an increased or decreased cost of fuel." [63] The Director of the Kansas Energy Office also urged the Legislature to prevent indefinite price escalator clauses from raising the price of old gas to the new gas incentive price, which was set artificially high to encourage new production.[64]

Representatives of labor unions, municipal utilities, and representatives of indvidual cities decried the unfair prices that these contract clauses could generate in NGPA markets in the absence of regulation. KPL testified before the Special Committee at the express request of the committee chairman, who sought information on the impact of the bill on customers of the state's largest utility.[65] Western Kansas farmers, who rely heavily on nat-

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[62] Office of the Governor of the State of Kansas, *Press Release* (May 7, 1979).

[63] *Minutes, May Hearings, supra* note 5 (statement of R. Loux, Attachments 7 & 23).

[64] "We are dealing with a limited number of people who see a very rare opportunity to make a very substantial sum of money, money not justified by additional work, additional investment, or additional risk, or even common sense, but by the strange hybrid interaction of old contract language and a new law. I see no reason why Kansas consumers should be forced by such circumstances to pay more for old Kansas gas than consumers in other states to which we currently export." *Id.* (statement of J. King, Attachment 8 at 1).

[65] *Minutes, May Hearings, supra* note 5 (statement of D. Black, Attachment 9 at 1).

ural gas for irrigation,[66] also affirmed the benefits of the legislation on agriculture in the state.[67]

The Special Committee heard detailed descriptions of the natural gas situation in Kansas and Oklahoma and the Oklahoma legislative response to the problem. The Committee examined documentary analyses of the gas markets and conditions in both states, and reviewed studies of gas production, reserves and market destination breakdowns in Kansas.[68] The Committee also considered the potential impact of NGPA ceiling prices on all gas in Kansas.[69] The Legislature determined that the Price Protection Act would, between 1979 and 1984, foreclose almost $128 million in additional gas costs, assuming 10% annual gas price increases under the NGPA.[70]

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[66] *See* 124 Cong. Rec. S14957 (daily ed. Sept. 12, 1978) (statement of Sen. Talmadge).

[67] *Minutes, May Hearings, supra* note 5, at 3. Kansas, Oklahoma and New Mexico are among seven states that account for 94% of all natural gas consumption used for irrigation. Congressional Research Service, Library of Congress, *Effects of Nutural Gas Decontrol on Farming Costs and Income* 6 (April 29, 1982). *See* Rep. K. Farrar, Memorandum, *A Brief Look at the Results of the Passage of the National Energy Act in Western Kansas*, April 27, 1979 (Copy on file in Legislative Research Department) (gas price increases are "a ripoff of the irrigator").

[68] Kansas Legislative Research Dep't, *Oklahoma Experience on Senate Bill No. 49, Report to the Special Comm. on Energy and Natural Resources* (May 9, 1979); R. Powers, *Production of Crude Oil and Natural Gas in Kansas*, Kansas Legislative Research Dep't (March 20, 1979); Kansas Energy Office and Kansas Corp. Comm'n, *Background Memorandum on H.B. 2680* (May 8, 1979); Kansas Legislative Research Dep't, *Overview of the Natural Gas Policy Act of 1978* 8-24 (March, 1979).

[69] Kansas Legislative Research Dep't, *The Effect of the Natural Gas Policy Act (NGPA) of 1978 on Kansas* (March 27, 1979).

[70] Special Comm. on Energy and Natural Resources, *Report on 1979 H.B. 2680*, J.S.App. pp. 71a, 73a. The actual rate of price increases under the NGPA ultimately proved to be significantly higher. See note 24, *supra*.

Representatives of eleven separate natural gas producers, and a representative of an association of over 1,000 independent oil and gas producers in Kansas, testified in opposition to the Bill.[71] Producers suggested that, if the legislation were enacted, they would refuse to explore for new natural gas in Kansas, terminate their contracts[72] and remove their gas from the state—a threat that the Legislature took seriously.[73] Producers also contended, without evidence, that the bill would benefit KPL and other utilities.

The Special Committee rejected these contentions and reported the bill favorably to both legislative bodies,[74] where, after amendment on the Senate floor,[75] the bill passed by overwhelming majorities.[76] Gas producers later obtained hearings before the Legislature to urge rescis-

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[71] *Minutes, May Hearings, supra* note 5, at 4-7.

[72] ERG erroneously argues that KPL testified that producers could terminate contracts if the Act passed. J.S. 21 n.34. KPL testified to the contrary, as did counsel for the KCC and the Governor's Office, and as a FERC opinion letter agreed. *Minutes, May Hearings, supra* note 5 (Statements of D. Black, L. Stroup, J. Martin, Letter of S. Balis, Attachments 9, 13, 24, 26).

[73] H.B. 2680 was amended before passage to require the KCC to monitor and report yearly intrastate natural gas supplies and production in Kansas. Senate and House Journals, *Proceedings of the Legislature of the State of Kansas*, 1979 Sess. S785-88 (May 14, 1979); Kan.Stat.Ann. § 55-1411 (Supp. 1980).

[74] Kansas Legislative Information System, *1979 Senate and House Actions Report* S98 (May 14, 1979); Special Comm. Report, *supra* note 70, J.S.App. 71a, 80a.

[75] The Senate considered six amendments to the Act; on roll call votes four passed and two were defeated. Senate and House Journals, *Proceedings of the Legislature of the State of Kansas*, 1979 Sess. S785-88 (May 14, 1979). ERG initially challenged the Act in reliance on minority members' statements that H.B. 2680 needed amendments that parliamentary tactics allegedly had precluded. J.S. 24; J.S.App. 85a. ERG now argues that the amendments, even though made, are irrelevant. Appt's Br. 11.

[76] The Senate vote was 36-3. The House vote was 92-31. Kansas Legislative Information System, *1979 Senate and House Actions*

sion of the Act.[77] The Legislature also studied the impact of the Act as reported by the KCC, however, and did not reverse its prior statutory decision.

As enacted, the Price Protection Act limits natural gas price increases under indefinite price escalator clauses, which otherwise could provide, without regard to market forces, unrestrained price increases in new market conditions of escalating price ceilings under the NGPA. The Act ties escalations for intrastate gas in Kansas to the corresponding NGPA ceiling prices for that same gas in the interstate market.

Like the NGPA, the Price Protection Act "concentrates the greatest price increases on those categories of gas where the potential for increasing supplies is the greatest." [78] The Act allows intrastate new gas to escalate to the § 102 price for new gas in the interstate market, and intrastate stripper gas to escalate to the § 108 price for stripper gas in the interstate market under the NGPA. The Act limits price increases on old intrastate gas in Kansas to the NGPA § 109 price, which equals the highest NGPA ceiling established for similar old gas in the interstate market under § 104.[79]

Report 98 (May 14, 1979). Only seven of the original dissenting members of the special committee voted against the bill. Senate and House Journals, *Proceedings of the Legislature of the State of Kansas*, 1979 Sess. S787, H973 (May 14, 1979).

[77] Kansas Legislative Research Dep't, *Minutes, Hearings Before the Senate Comm. on Energy and Natural Resources* (February 20, 1980).

[78] *Economic Analysis of the NGPA*, *supra* note 24, at 2.

[79] Kan. Stat. Ann. §§ 55-1405, -1406. This Act allows price increases to the NGPA § 109 price only in accordance with the terms of parties' contracts. Because ERG's price redetermination clause authorizes price increases once every two years, and because the Courts below held that the "government pricing" clause did not trigger higher prices in conjunction with NGPA enactment, ERG's contract price adjusts to the § 109 price only on redetermination dates.

D. The Litigation Below

On June 5, 1979, 85 days after FERC withdrew its interim regulations,[80] ERG gave notice that it was terminating its contracts pursuant to their terms. ERG filed the instant action for a declaratory judgment that it terminated the contracts in July 1979 because of KPL's failure to pay the § 102 price under its government pricing clause, and in August 1979 because of KPL's alleged breach in later refusing to redetermine to that price. The Court below held that mere enactment of the NGPA did not "fix a higher price" sufficient to trigger a price increase under the government pricing clause, and thus no contract right to terminate arose in July 1979. The Kansas Act constitutionally restricted the price increase under the redetermination clause to the § 109 price, then below ERG's contract price, and thus no breach occurred in August. J.S.App. 23a-24a. The Court affirmed the judgment against ERG. J.S.App. 24a, 49a.

SUMMARY OF THE ARGUMENT

ERG executed intrastate contracts that permitted future, indefinite price escalations "subject to all future state laws." In December 1978 the NGPA established for intrastate natural gas a tentative price ceiling, subject to state authority to restrict contract clauses that could escalate prices up to that ceiling. In May 1979 Kansas enacted intrastate price control legislation similar to that previously enacted in Oklahoma and New Mexico. ERG otherwise would have been entitled to redetermine its contract price, effective November 1979, up to the NGPA § 102 new gas incentive price. The Price Protection Act, however, restricted price redeterminations for ERG's old

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Thus, ERG's reference that it currently receives "less than the § 109 price," Appt's Br. 22-23, in actuality means that ERG receives adjustments to the § 109 price in conformity with its contracts.

[80] FERC Order No. 23, 44 Fed. Reg. 16899 (March 20, 1979). ERG's contracts required that it wait 75 days after the effective date of any price increase under the government pricing clause before any right of termination would arise. J.S.App. 69a.

gas to the NGPA § 109 price ceiling. It thus prospectively prohibited the 1979 redetermination.

1. The Price Protection Act is legitimate price control legislation which, under *Home Building & Loan Ass'n. v. Blaisdell*, 290 U.S. 398 (1934), does not violate the Contract Clause of the Constitution.

(a) The Act serves the important, legitimate state goal of regulating intrastate natural gas prices. The debate on appropriate gas pricing policy arises from the impact of artificially high, OPEC-controlled oil prices that compel higher prices for natural gas. The NGPA endorses continued price regulation to control the economic conditions that these prices create, and reserves to the states an important role in achieving a responsible pricing policy. The NGPA specifically contemplates state regulation of indefinite escalator clauses, which admittedly produce market distortions, and which continue to be the subject of frequent regulatory attention.

(b) Consistent with *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234 (1978), and *United States Trust Co. v. New Jersey*, 431 U.S. 1 (1977), the Kansas Act is both a necessary and a reasonable means to achieve the Kansas goals of limiting price increases for old intrastate natural gas, stimulating new gas production, and minimizing any adverse impact on affected producers. Complementing the NGPA, the Act effectively imposes for intrastate gas the same NGPA price ceilings available in the interstate market.

Rather than the "unfounded benefits" that ERG alleges "could not begin to solve the problems" of higher prices, the Act provides savings, *undisputed* by ERG, of more than $128,000,000 in increased gas costs to Kansas consumers, together with additional savings, perhaps equally great,[81] from the impact of those costs

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[81] *See* Congressional Budget Office, *The Effect Of OPEC Oil Pricing On Output, Prices And Exchange Rates In The United*

on other goods. The Act still allows ERG a price almost eight-fold higher than the average price in Kansas ten years before. The Act only denies ERG a "market value" that all agree is far above any competitive market price for that natural gas.[82]

(c) In any event, ERG cannot allege a serious statutory impairment of its contracts when those contracts expressly incorporate future state laws regulating the contractual price terms. *White v. United States*, 270 U.S. 175 (1926). ERG's contract clauses only guarantee price increases subject to future state laws. This is the price that ERG presently receives, a price that ERG never claimed below was unreasonable or unprofitable. As the federal government either returns to the states more responsibility for economic and social regulatory functions, or joins with states in a partnership to perform those functions, this Court should be extremely cautious to impose, through the Contract Clause, new constitutional constraints on states' abilities to meet these responsibilities.

2. Congress expressly declared that it did "not intend that the mere establishment of the ceiling prices under [the NGPA] shall trigger indefinite price escalator clauses in existing intrastate contracts."[83] ERG nevertheless claims that "the mere establishment of NGPA ceiling prices" triggered its government pricing clause,

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States and Other Industrialized Countries (February, 1982); *Economics Of The Gas Controversy*, *supra* note 9, at 59-61, 69; 124 Cong. Rec. S14874 (daily ed. Sept. 11, 1978) (statement of Sen. Metzenbaum); *Hearings on Implementation Of Title I*, *supra* note 17 at 172-73 (statement of R. Mitchell).

[82] *Hearings on Proposed Energy Plan*, *supra* note 14, at 6, 18, 21 (statement of J. Schlesinger); *Economics of the Gas Controversy*, *supra* note 9, at 76; 124 Cong. Rec. S14951 (daily ed. Sept. 12, 1978) (statement of Sen. Hollings). The average gas price in Kansas in 1972 was $0.32 per Mcf. *Minutes, May Hearings*, *supra* note 5 (statement of L. Stroup).

[83] H.R. Rep. No. 1752, *supra* note 46, at 83.

which provides higher prices if Congress "fixes a higher price" for Kansas gas. The Court below correctly ruled that Congress did not "fix a higher price," within the meaning of this clause, when it established as a ceiling for Kansas gas merely "the terms" of ERG's contracts.

ARGUMENT

I. THE PRICE PROTECTION ACT LEGITIMATELY ADDRESSES A TRADITIONAL AND BONA FIDE STATE GOAL AND IS NOT SPECIAL LEGISLATION

The principal question presented on this appeal is whether the price control provisions of the Price Protection Act violate the Contract Clause of the United States Constitution. ERG understandably attempts to posture this question as more than a customary constitutional challenge to legislative regulation that either deprives it of a reasonable price for its property, or alters the price terms of its contracts for the sale of that property.

Price controls in this country date back more than two centuries.[84] "A legislative power to create price ceilings has, in 'countries where the common law prevails' been 'customary from time immemorial. . . .' Its exercise has regularly been approved by this court." [85] The existence of this state constitutional power to regulate prices "in the last half century made possible, within a selected field, a degree of experimentation in governmental direction of economic activity of vast import and beyond any historical parallel." [86] Reliance on this power

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[84] Aiton, *Early American Price Fixing Legislation*, 25 Mich . L. Rev. 15 (1926); Hayes, *Business Regulation in Early Pennsylvania*, 10 Temp. L. Q. 155 (1936). *See also* Strong, *The Economic Philosophy of Lochner: Emergence, Embrasure and Emasculation*, 15 Ariz. L. Rev. 419 (1973).

[85] *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 768-69 (1968) (quoting *Munn v. Illinois*, 94 U.S. 113 (1876)).

[86] F. Frankfurter and H. M. Hart, *Rate Regulation*, in *Crises of the Regulatory Commissions* 2 (P. MacAvoy ed. 1970).

"grew into one of the most significant legislative developments of the 20th Century." [87]

Exercise of this traditional power in the field of natural gas regulation, "a subject which especially comes within [a state's] lawful authority," [88] is well established. This Court has already affirmed "the power of a state to fix prices at the wellhead on natural gas produced within its borders." [89] In numerous contexts this Court has already upheld as constitutional state regulation of, and price controls on, intrastate natural gas.[90] "The price of gas distributed through pipelines for public consumption has been . . . long and consistently recognized as a proper subject of [state] regulation." [91]

State exercise of this legislative power was appropriate in the face of the sudden price increases anticipated under the NGPA.[92] In response to the acknowledged problem of indefinite escalator clauses in intrastate NGPA markets, both Oklahoma and New Mexico also enacted or extended price control legislation restricting intrastate price increases.[93]

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[87] *Id.*

[88] *Ohio Oil Co. v. Indiana*, 177 U.S. 190 (1900).

[89] *Cities Service Gas Co. v. Peerless Oil & Gas Co.*, 340 U.S. 179, 180 (1950).

[90] *Railroad Comm'n v. Rowan & Nichols Oil Co.*, 310 U.S. 573 (1940); *Railroad Comm'n v. Pacific Gas Co.*, 302 U.S. 388 (1938); *Champlin Refining Co. v. Corporation Comm'n*, 286 U.S. 210 (1932); *Cedar Rapids Gas Light Co. v. City of Cedar Rapids*, 223 U.S. 655 (1912); *Willcox v. Consolidated Gas Co.*, 212 U.S. 19 (1909).

[91] *Federal Power Comm'n v. Natural Gas Pipeline Co.*, 315 U.S. 575, 582 (1942) (citing *Railroad Comm'n v. Pacific Gas Co.*, 302 U.S. 388 (1938)).

[92] *See Impact of Natural Gas Prices on Consumers: Hearings Before the Subcomm. on Intergovernmental Relations of the Sen. Comm. on Governmental Affairs*, 96 Cong., 1st Sess. 9, 292 *et seq.* (1979) (statements of C. Curtis, Chairman, FERC, and Sen. Sasser).

[93] Okla. Stat. Ann. tit. 52, §§ 260.1-.13 (1979); N. Mex. Stat. Ann. §§ 62-7-1 *et seq.* (Supp. 1981).

ERG thus challenges the Kansas Act on the basis of alleged legislative and corporate impropriety, which allegedly sought to protect KPL "profits" and award KPL "enormous benefits" by forbidding gas cost increases that KPL "probably" would absorb. Appt's Br. 31-32. ERG ignores the fact that the KCC adopted in 1977 a PGA clause that authorized the immediate pass-through to consumers of all increased costs for natural gas. Even before the Legislature convened in 1979, the PGA directed KPL to pass through increased gas costs without applying for the review and hearing that ERG's contracts contemplate for adjustments to KPL's operating expenses. KPL did *not* stand to gain financially from legislative restrictions on wellhead gas costs. The KCC so noted. App. 8. The KCC, the Kansas Energy Office, KPL and other utilities so testified, or so stated by implication, before the Legislature.

Even without the PGA, state legislation that effectively limits a utility's operating expenses could not affect the utility's rate base and rate of return. ERG simply misunderstands utility rate regulation. By definition, operating expenses do not form any part of, and cannot affect, a utility's rate base, which consists *solely* of the current property—plant and equipment—"used or required to be used" to serve the public. Kan. Stat. Ann. § 66-128 (1980). Operating expenses also have no bearing on the rate of return that the KCC in its discretion permits a utility the opportunity to earn.[94] Whether KPL passed through gas cost increases or "prevent[ed] price increases in the first instance," Appt's Br. 33, made absolutely *no* difference to KPL's established rate base or its allowed rate of return.

Moreover, by arguing that KPL would "probably" absorb gas cost increases, ERG argues that § 102 prices are not "just and reasonable" expenses that a utility nec-

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[94] 1 A. Priest, *Principles of Utility Regulation*, 45, 50-51, 139 *et seq.* (1969).

essarily recovers as a matter of law.[95] ERG claims entitlement to a § 102 price, however, precisely because that price *is* "just and reasonable" and allegedly does *not* violate public policy.

Neither the history nor the impact of the Kansas Act supports ERG's contention that the Act serves an illegitimate goal. The Legislature began consideration of natural gas price controls within the first weeks of its first legislative session after NGPA enactment. Unlike *Allied Structural Steel*, where employees of one of two affected companies petitioned the legislature for pension relief, the Act here was placed before the Legislature by Governor Carlin, who, citing support from "Federal and State regulatory agencies and various major utilities," described the Act as important and beneficial to Kansas consumers.[96]

The legislative path followed by Kansas reflected a deliberate and continuing examination of alternatives in natural gas pricing. Legislative attention to these specific price controls spanned more than twelve months with five days of hearings on three separate occasions. Legislative records in Kansas included hundreds of pages of testimony and documents, agency investigations and reports. The Act resulted from the Legislature's studied effort to deal with a problem of both national and state concern; it was not "too hastily adopted." [97]

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[95] *Id.*

[96] "It is imperative that this legislation be debated on its merits and that the full legislature have the opportunity to vote this measure up or down. I am certain that upon further study you will be as convinced as I am that the passage of this measure is unquestionably in the best interest of the Kansas utility consumer. In the past weeks, the Kansas Energy Office, Federal and State regulatory agencies, and various major utilities have jointly indicated the need for such legislation." Office of the Governor, *Letter to R. Doyen*, Chairman, Legislative Coordinating Counsel (May 3, 1979).

[97] Appt's Br. 20. Indeed, ERG previously argued that the Legislature did not adopt the statute quickly enough, contending that, had "[the NGPA] caused a true emergency within the meaning of

"[E]nergy policy in general has not proved to be an easy task . . . it can rarely be isolated from other concerns, and cannot be addressed as a single episode or need." [98] Natural gas is perhaps the single most important energy source for the agricultural industry,[99] and legislative attention to gas prices in Kansas is doubtless not yet finished, a point that ERG indirectly concedes.[100]

ERG claims that the Kansas Act cannot address a legitimate purpose because it regulates "only" price increases under indefinite escalator clauses. Regulation of these clauses in interstate contracts has, however, been traditionally approved.[101] Regulation is even more appro-

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Blaisdell," the Kansas Legislature would have acted on the statute sooner than it did. J.S. 17.

[98] Congressional Research Service, *U.S. Energy Outlook: Demand Perspective for the Eighties, Report to the House Comm. on Energy and Commerce*, 97th Cong., 1st Sess. 583 (Comm. Print 1981).

[99] "[T]he farmers are the biggest consumers [of natural gas] of all." 124 Cong. Rec. S16131 (daily ed. Sept. 26, 1978) (statement of Sen. Dole). *See also* 124 Cong. Rec. S14957 (daily ed. Sept. 12, 1978) (statement of Sen. Talmadge); *Hearings on Deregulation, supra* note 17 at 50 (statement of V. Steffen). More than 60% of the total domestic production of nitrogen fertilizer in America is manufactured through use of intrastate natural gas. *Hearings on Implementation of Title I, supra* note 17, at 423 (statment of D. Willis); *Minutes, May Hearings, supra* note 5, at 3. (testimony of F. Troutman, Southwest Kansas Irrigators Ass'n).

[100] Appt's Br. 39 n.53. Governor Carlin has more recently proposed an absolute freeze on all intrastate natural gas prices. State governors recently adopted Governor Carlin's resolution to urge Congress to address the "harmful effects" of indefinite escalator clauses in interstate contracts. Office of the Governor of the State of Kansas, *Press Releases* (March 19, Aug. 5, 1982); National Governors' Ass'n, *Amendments to Position on Natural Gas Policy* (Aug. 10, 1982). The Legislature has also considered a statute that would allocate to elderly Kansans the benefits of restricted old gas prices. S.B. 885, Kansas Legislative Information System, *1982 Senate and House Actions Report* S105 (April 30, 1982).

[101] *In re Permian Basin Area Rate Cases*, 390 U.S. 781-84 (1968); *Federal Power Comm'n v. Texaco, Inc.*, 377 U.S. 33 (1964). *See also* Comment, *The FPC and Indefinite Price Escalation Clauses:*

priate in the intrastate market under the NGPA.[102] These clauses "lead to prices higher under the NGPA than we would see in any kind of free market or . . . set by the competing fuels." [103] Indeed, the Conferees only agreed on the NGPA after a specific acknowledgment of the propriety of these state restrictions.

ERG alleges that Senators Tower and Bentsen and Representative Brown did not anticipate state restrictions on escalator clauses. Appt's Br. 24 n.32. The cited remarks, however, supported the Pearson-Bentsen deregulation bill, which Congress rejected, and criticized a plan to extend, to the previously unregulated intrastate market, an April 1977 new gas ceiling of $1.75 per Mcf, a provision that NGPA § 102 ultimately incorporated.[104] Contrary to ERG's contention, Senator Bentsen actually *favored* regulation of indefinite price escalator clauses in intrastate contracts.[105]

Constitutional authority to regulate these clauses will become even more significant in 1985. With partial NGPA deregulation and an anticipated price "fly-up" of 50% to 150%, operation of indefinite escalator clauses could cost consumers an additional $29 billion in increased gas costs, "creating a domino effect of higher prices" and

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Remedy for an Administrative Breakdown, 73 Yale L.J. 1283, 1290-93 (1964).

[102] See notes 27-31 *supra*. *Hearings on Implementation of Title I*, *supra* note 17, at 337 (statement of G. Lawrence); *Natural Gas Option-New Resources and New Technologies, Hearings Before the Subcomm. on Energy Development and Applications of the House Comm. on Science and Technology*, 97th Cong., 1st Sess. 105, 107 (1981) (statement of R. Willis).

[103] *Hearings on Implementation of Title I*, *supra* note 17, at 110 (statement of Dr. Cicchetti). *See also Id.* at 14, 332 (statements of C. Butler, chairman, FERC, and G. Lawrence).

[104] 123 Cong. Rec. 25912, 30384, 30397, 30736 (1977) (statements of Sens. Tower and Bentsen and Rep. Brown). These members all thus voted against the NGPA. 124 Cong. Rec. S16265 (daily ed. Sept. 27, 1978); 124 Cong. Rec. H13427 (daily ed. Oct. 14, 1978).

[105] *Hearings on S. 256*, *supra* note 17, at 486 (statement of Sen. Bentsen).

producing "severe economic effects." [106] For this reason, even FERC recently inquired into proposed new restrictions on the operation of these clauses,[107] an action that it later postponed when consumer groups sought thereby to freeze or roll back current NGPA prices.

ERG simply cannot dispute that intrastate natural gas price regulation is a legitimate state goal. The NGPA is premised on the idea that the domestic natural gas market does not conform to classical theories of free competition,[108] and that even if it did, OPEC market domination requires controls on artificially inflated natural gas prices.[109] The Kansas Act merely acknowledges the Federal view that "unchecked natural gas prices . . . would result in potentially massive profits for producers and would cause reductions in real income to consumers and inflationary pressures on the economy." [110] Although ERG

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[106] *Hearings on Implementation of Title I, supra* note 17, at 334, 197-99 (statements of G. Lawrence, J. Elam); C. Abbott, *Natural Gas Markets in the Transition to Decontrol*, in *Amendments to the Power Plant and Industrial Fuel Use Act, Hearings on S.332 and S.410 Before the Subcomm. on Energy Regulation of the Senate Comm. on Energy and Natural Resources*, 97th Cong., 1st Sess. 488, 503 (1981).

[107] Federal Energy Regulatory Commission, *Notice of Inquiry: Impact of the NGPA on Current and Projected Natural Gas Markets*, Docket No. RM82-26-000, 47 Fed. Reg. 19157 (May 4, 1982). *See Hearings on Implementation of Title I, supra* note 17, at 110, 116-17, 122, 197-99, 332-37, 359, 444, 601 (statements of Dr. Cicchetti, J. Elaim, G. Lawrence, E. Luntey, D. Willis, P. Barber).

[108] *Economic Analysis of the NGPA, supra* note 24, at 5. This premise is independent of whether monopolistic barriers inhibit entrance into the market. *See Pennzoil, supra*, 645 F.2d at 378.

[109] 124 Cong. Rec. H13149-50, H13418, H13420 (daily ed., Oct. 14, 1978) (statements of Reps. Scheuer, Dornan & Harris); *Hearings on Proposed Energy Plan, supra* note 14, at 18 (statement of J. Schlesinger); *Hearings on S.256, supra* note 17, at 150 (statement of E. Berlin).

[110] *Hearings on Proposed Energy Plan, supra* note 14, at 6 (statement of J. Schlesinger). Unrestricted prices could generate

maintains that legislation providing only "a modicum of [price] restraint" cannot, by definition, address any legitimate purpose, Appt's Br. 16, 30-31, that "modicum" of relief to the poor may constitute a significant percentage of their disposable income and make the difference between hardship and tragedy.[111]

ERG seeks to impeach a legitimate legislative intent by relying on KPL's public support for responsible intrastate pricing policies, and on the same factual contentions that the Legislature rejected. ERG cites the statements of three minority members, who, with substantial contributions from the oil and gas industry,[112] merely repeated

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additional inflation of 3 or 4 percentage points and cost the economy tens of billions of dollars. American Gas Association, *Cost of Immediate Price Decontrol of Natural Gas to Low Income and Disadvantaged Groups*, in *Energy and the Aged; Hearings Before the Senate Special Comm. on Aging*, 97th Cong., 1st Sess. 150 (1981); *Economics of the Gas Controversy*, *supra* note 9, at 39, 69; 124 Cong. Rec. S14874 (daily ed. Sept. 11, 1978) (statement of Sen. Metzenbaum).

[111] After the government forecast that increased gas prices would threaten many elderly with the prospect of inadequately heated homes, *Energy and the Aged, Hearings Before the Senate Special Comm. on Aging*, 97th Cong., 1st Sess. 176, 180-84 (1981) (statement of D. Elliott), record cold killed more than 600 people, many of whom died, as did many elderly during the heat wave in 1980, because they feared incurring an additional "modicum" of utility costs to maintain safe room temperatures. *Energy Assistance for the Elderly (Impact of the 1980 Heat Wave), Joint Hearings Before the Senate Special Comm. on Aging and the Subcomm. on Aging of the Senate Comm. on Labor and Human Resources*, 96th Cong., 2d Sess. (pt. 4) 289, 291, 318 (1980) (statements of D. Baumgardner, Sens. Chiles and Eagleton). *See Energy and the Aged; Hearings Before the Senate Special Comm. on Aging*, 97th Cong., 1st Sess. 150 (1981); *Energy Equity and the Elderly in the 80's, Hearings Before the Senate Special Comm. on Aging*, 96th Cong., 2d Sess. (pts. 1-2) (1980) (unrestricted natural gas costs would consume 20% of the gross income of the poor).

[112] Kansas Governmental Ethics Commission, *Receipts and Expenditure Reports filed with the Secretary of State*, Topeka, Kansas, 1980 Reports of Sens. P. Hess, C. Angell, and W. Sowers.

the unsupported claims of producers that the Kansas Act would benefit utilities. Legislative purpose cannot be determined by remarks of a small minority. The NGPA was also described by critics, including some who "reluctantly voted for the bill," as a "boon" to the "giant oil companies," "a tremendous hoax," and a "dishonest effort" that was too hastily rushed through Congress for improper reasons.[113]

Even had KPL proposed and benefited from the Kansas Act, the Act still serves a legitimate goal. The state law could not be set aside solely "because of the fact, if it be such, that it ha[d] been sponsored and promoted by those who advantage from it." [114] Before the Legislature, ERG did not dispute the significant savings of the Kansas Act. In a state with a $2 billion annual budget,[115] this public benefit is hardly the "insignificant" governmental act that ERG describes. The Act satisfies constitutional requirements by addressing a legitimate state concern, and should be upheld on that basis.

II. THE PRICE PROTECTION ACT IS REASONABLY RELATED TO ITS LEGITIMATE GOAL AND DOES NOT SUBSTANTIALLY IMPAIR ERG'S CONTRACTS

The Contract Clause is not offended by "legislation adjusting the rights and responsibilities of contracting parties upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption." *United States Trust Co. v. New Jersey*, 431 U.S. 1, 22 (1977). Contract Clause analysis under *Blaisdell* and

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[113] 124 Cong. Rec. H13132, H13136, H13138, H13145, H13238, H13420 (daily ed. Oct. 14, 1978) (statements of Reps. Kemp, Ottinger, Harris, Livingston, Krueger and Brown); 124 Cong. Rec. 29389, 30016 (1978) (statements of Sens. Goldwater and Abourezk).

[114] *Cohen v. Beneficial Industrial Loan Corp.*, 337 U.S. 541, 550-51 (1949).

[115] *See* Office of the Governor of the State of Kansas, *Governor's Legislative Message and Budget Report* 3 (Jan. 23, 1979).

Allied Structural Steel addresses the importance of the legislative goals [116] and the reasonableness of the statutory provisions as related to these goals.[117] Regardless of the Act's legitimate purpose, ERG assails the Kansas Act as insufficiently related to that purpose.

A. The Provisions of the Act are Reasonably Related to the Statutory Goal

The Kansas Act addresses the same goal that underlies the NGPA: gradual introduction of higher gas prices in a manner that "assures that economic health is maintained and improved, that unemployment rates are reduced, and that inflationary pressures are minimized." [118] Kansas has thus adopted an intrastate pricing system that closely resembles the Federal pricing system for interstate gas. As ERG confirmed to the Legislature, the Kansas Act supports the NGPA goal of equalizing interstate and intrastate market prices.[119]

1. *The Reasonableness of the Provisions*

The Kansas Act provides that indefinite escalator clauses for old gas may operate, if their terms so provide, up to the escalating § 109 price, which equals the highest NGPA price for old gas in the interstate market.

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[116] Two *Blaisdell* factors address this determination: whether an emergency exists and whether the statute protects a basic societal interest.

[117] The remaining three *Blaisdell* factors address these concerns: whether the legislation is appropriately tailored to the problem it addresses, whether the legislative remedy is limited in duration, and whether the legislation contains reasonable conditions.

[118] *Economic Analysis of the NGPA, supra* note 24, at 2.

[119] *See* Id. at 8-10. One ERG officer testified that, by suppressing intrastate prices, the Kansas Act diverts gas into the interstate markets and "plays right into the hands of the eastern consuming states whose representatives were the major architects [of § 105] and whose intent was to take gas away from producing states." *Minutes, May Hearings, supra* note 5 (statement of D. Smette, at 2-3, Attachment 18).

Kan. Stat. Ann. § 55-1405 (Supp. 1980). ERG challenges this provision because it bars receipt of a § 102 new gas price for its old intrastate gas under contract. ERG, however, never claimed below that this "artificially low [§ 109] price," Appt's Br. 11, denies it significant profits. Indeed, ERG declared "reasonable" the Federal imposition, under §§ 105 and 106, of even *lower* prices on much old *intrastate gas* not subject to indefinite escalator clauses.[120]

ERG assails the Act as unreasonable because the Act contains limitations to reduce its impact on producers' contracts. ERG concedes that the Act would be constitutional if it absolutely fixed a single, non-escalating price for all intrastate gas, without exception, thus *reducing* ERG's present contract price and *barring* ERG from receiving high stripper well prices for stripper well gas. J.S. 22 n.35. If such severe legislation is constitutional, the lesser impairment involved here necessarily satisfies the *Allied* standard. "The severity of the impairment measures the height of the hurdle the State legislation must clear." *Allied, supra*, 438 U.S. at 245.

The challenged statutory exceptions "reasonably tailor" the Kansas Act to NGPA contours. *Allied, supra*, 432 U.S. at 242. Like the Oklahoma and New Mexico statutes, the Kansas Act permits for new and stripper well gas the same incentive price that the NGPA allows in the interstate market.[121] Although ERG alleges that this feature creates a "narrow statutory focus" that is "damning," the Contract Clause requires that a statute be no more restrictive than is reasonably necessary to achieve its

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[120] Plaintiff's Memorandum Filed Feb. 4, 1980, at 21, R. Vol. II at 85; *See, e.g., Ecee, Inc. v. FERC*, 645 F.2d 339, 356-59 (5th Cir. 1981) (party seeking § 109 ceiling instead of lower § 105 price).

[121] *See, e.g.*, N. Mex. Stat. Ann. §§ 62-7-6 to -7-9 (Supp. 1981).

purpose.[122] Without these exceptions, the Act would more nearly demonstrate the "utter indifference to the legitimate interests of other parties" that ERG so often assails. Appt's Br. 20.

ERG misleadingly contends that the Act unreasonably regulates an insufficient volume of Kansas gas. The NGPA specifically reserves to the states, and the states only possess, constitutional authority to regulate intrastate gas prices.[123] Moreover, old interstate gas prices remain *lower* than the § 109 price, and thus do not pose the threat of the unreasonable price increases that ERG seeks.

ERG concedes that approximately 25% of Kansas gas consumption is intrastate gas subject to State control. Appt's Br. 30 n.42. Sixty percent of this gas is not subject to indefinite price escalator clauses. Under NGPA § 105, this gas is frozen to existing price terms and cannot, by renegotiation or otherwise, generate prices even approaching the § 102 level. The Kansas Act addresses, with "surgical precision," that 40% share of intrastate gas that *is* subject to indefinite escalator clauses,[124] and which alone has the potential for sudden, substantial price increases in conjunction with the NGPA. Fixed price escalator clauses in Kansas simply pose no threat of the massive price increases potentially generated by indefinite escalator clauses in conjunction with the NGPA. ERG's bald statement that fixed price escalator clauses "can lead to prices as high as [the § 102] ceiling," J.S. 23, is patently untrue. The Legislature could reasonably so conclude from the contracts submitted to it.[125]

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[122] Appt's Reply to Motion to Dismiss, 3 n.6. A state may not impose "a drastic impairment when an evident and more moderate course would serve its purposes equally well." *United States Trust Co. v. New Jersey*, 431 U.S. 1, 30-31 (1977).

[123] H.R. Rep. No. 1752 *supra* note 46, at 125; *Panhandle Eastern Pipeline Co. v. Public Serv. Comm'n*, 332 U.S. 507 (1947).

[124] See Special Committee Report, *supra* note 70, J.S.App. 73a.

[125] Those contracts, and those submitted by producers in 5 separate Kansas cases, contain fixed escalations of approximately $.02

If, as ERG contends, the Constitution requires that price controls affect a large percentage of total gas consumed in the state, or a large number of purchasers, the 13 producing states [126] with *less* production than Kansas could *never* regulate the price for the natural gas they produce. Indeed, price controls in New Mexico similarly address only the 10% to 18% intrastate share of that state's gas production, and generate annual cost savings of approximately $22 million, a figure comparable to that in Kansas.[127] If the Constitution requires that wellhead price controls affect numerous different purchasers, *no* state could implement controls. The only significant purchasers of intrastate gas at the wellhead are regulated utilities. Virtually by definition, they will be few in number.[128] The rationale of *Allied*, on which ERG relies, is simply inapposite here, where the "few" affected companies are regulated by the state to serve virtually all citizens.[129]

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every one to five years, on top of base contract prices of less than $2.00—an annual 1% price increase or less. *Minutes, May Hearings, supra* note 5 (Attachments 27, 29-32). To provide the § 102 price, a fixed escalation clause must adjust prices monthly, first by more than 15% just to reach the § 102 price, and thereafter by a percentage that coincidentally matches the inflation rate plus 4%.

[126] These include California, Colorado, Wyoming and Montana. Department of Energy, Energy Information Administration, *Energy Data Report* (March 4, 1982).

[127] G. Cibas, *Economic Impact on New Mexico of the Natural Gas Policy Act of 1978 and the New Mexico Natural Gas Pricing Act*, New Mexico Energy Management Information System, State Energy and Minerals Department 81, 248 (1981). New Mexico permits incentive prices for new and stripper gas, and, to reduce incentives to commit gas to interstate markets as intrastate contracts expire, for gas under new intrastate contracts. *Id.*

[128] In New Mexico, a single company purchases the vast share of the controlled intrastate gas. *Id.* at 54.

[129] ERG further challenges § 8 of the Kansas Act on the basis of alleged arbitrariness in allowing parties to renegotiate price provisions in contracts. Whatever the fairness of this provision, KPL has not made any demands on ERG to "dictate" new terms, and ERG has no standing to complain that this section has in any way altered its contractual obligations.

2. *The "Necessity" Standard of* United States Trust

ERG argues that the Price Protection Act is "unnecessary," within the meaning of *United States Trust*, because alternatives were available that would achieve the same objectives but less severely impair producers' contracts. The Kansas Legislature allegedly should have applied to KPL "incremental pricing" rules similar to those in NGPA Title II. Appt's Br. 37. Because it purchases interstate gas at the border for distribution within Kansas, however, KPL already *is* within Federal incremental pricing rules.[130] In any event, the KCC has *already* implemented, in its rate design structures for Kansas utilities, "a form of incremental pricing consistent with the NGPA." [131]

ERG also recommends that Kansas could better achieve its goals by denying utilities the right to pass through these higher gas costs to their consumers. ERG understandably did not pursue this claim in the trial court. Gas costs now typically constitute 50% to 60% of a utility's total operating expenses, and may by 1985 constitute 80% of those expenses.[132] ERG cannot seriously contend that a utility could absorb, without rate increases, a 20% to 25% annual increase in a cost item of this size. Denial of a pass-through, even if it were lawful, would require that these contracts be terminated, as ERG desires. ERG's true alternative to a responsible pricing policy is simply that, if Kansas seeks to regulate gas prices, then Kansas citizens should survive without natural gas.

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[130] *See* 15 U.S.C. § 3344(c)(4) (1982); 18 C.F.R. § 282.103(b) (1981); 124 Cong. Rec. S15598 (daily ed., Sept. 25, 1978) (statement of Sen. Bartlett); see also Special Committee Report, *supra* note 70, J.S.App. 81a.

[131] *Midwest Gas Users' Ass'n v. State Corp. Comm'n*, 5 Kan.App. 2d 653, 623 P.2d 924, 927 (1981).

[132] *Hearings on Implementation of Title I*, *supra* note 17, at 368 (statement of E. Luntey).

Past state regulation of natural gas has not been deemed inconsistent with the Contract Clause.[133] ERG concedes that states may regulate gas prices under contracts with a "state-sanctioned monopoly whose rate-making process [is] a public one," when complaining parties are on "fair notice" of possible rate restrictions and have the opportunity to be heard. Appt's Br. 33-34 n.47. This is no distinction. ERG "freely entered" these contracts with a "state-sanctioned monopoly" subject to legislative regulation that has given ERG and other producers three opportunities to be heard. The Kansas Act should not be set aside here.

B. The Act Does Not Substantially Impair ERG's Contracts

ERG's claim of a severe contractual impairment presupposes that the *unregulated* operation of the indefinite price escalator clauses is "crucial" to ERG's contractual expectations. ERG's claim repudiates its own contractual agreement that its escalator clauses could provide natural gas prices no higher than State policy would allow. ERG's indefinite price escalator clauses expressly incorporate all future state laws. J.S.App. 69a-70a. ERG "was substantially induced to enter into these contracts," Appt's Br. 27, solely on the basis of KPL's promise to pay a contract price *controlled by state regulation.* KPL in fact pays that increased price.

ERG contends that its contracts do not so provide. ERG argues that it may terminate its contracts if state law prohibits "bargained-for-price increases" that are the precondition to the right to terminate. Appt's Br. 26 n.36. The "bargained-for" price increases are, however, those provided in the escalator clauses that *are* expressly

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[133] *See, e.g., Palmer Oil Corp. v. Amerada Petroleum Corp.*, 343 U.S. 390 (1950); *Henderson Co. v. Thompson*, 300 U.S. 258, 266 (1937); *Bandini Petroleum Co. v. Superior Court*, 284 U.S. 8, 22 (1931); *Fort Smith Spelter Co. v. Clear Creek Oil & Gas Co.*, 267 U.S. 231 (1925).

subject to future state laws.[134] KPL has promised in these contracts to pay price increases subject to state law, and ERG retains the right to terminate its contracts if KPL refuses to pay those price increases permitted by state law. The contracts specifically provide "that neither party shall be held in default for failure to perform hereunder if such failure is due to compliance with such laws." J.S. App. 70a. Both courts below so held. J.S. App. 16a, 24a, 34a.

ERG further argues that its contracts do not adopt state laws that are unconstitutional. Though this argument may have validity under other constitutional challenges, the argument cannot stand in a Contract Clause claim. When a contract incorporates a state law, that law by definition does not impair contractual obligations and no claim of unconstitutional impairment can even arise, as the Court in *Edmiston* held.[135]

ERG misstates the impact and function of its escalator clauses. ERG admits that inclusion of these clauses was a precondition to the execution of these contracts. With more than one-third of all interstate contracts and the vast majority of intrastate contracts containing indefinite escalator clauses,[136] their inclusion does not result, as ERG self-servingly represents, Appt's Br. 3, 24-25, in lower initial contract prices for natural gas.

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[134] The termination *procedures*, which arose upon price increases consistent with state law, were not expressly subject to state law. J.S.App. 70a. KPL thus conceivably had the duty, notwithstanding adoption of the PGA, to petition the KCC for a pass-through of any price increase. KPL did so petition to avoid claims of breach raised by producers obviously eager to terminate their contracts as gas prices soared.

[135] *Edmiston v. State Corp. Comm'n*, No. 79-1335, slip op. (D. Kan. Nov. 24, 1980), *as modified*, *id.* (D. Kan. Jan. 13, 1981), *appeal docketed*, No. 81-1197 (10th Cir. Feb. 23, 1981). *See White v. United States*, 270 U.S. 175 (1926).

[136] *Economics of the Gas Controversy*, *supra* note 9, at 84-85.

One study has already so concluded.[137] The presence of the clauses in all of the Spivey contracts is more an indication of the "tremendous market power that producers have over distributors," [138] than of the "free negotiations" that ERG represents. ERG argues that, without these clauses, "many . . . wells would not have been drilled," Appt's Br. 26, yet the wells under these contracts were drilled between 1954 and 1961, before ERG obtained the protection of these clauses, and since ERG obtained these clauses in 1975, ERG in fact has not drilled a single additional well.[139]

ERG's "substantial impairment" must be put into perspective. ERG purported to terminate its contracts in July 1979 when it failed to receive § 102 prices of $2.078 to $2.177 per Mcf. The NGPA § 109 price, available if contracts provide for price adjustment in October 1982, is $2.224, which ERG contends is "artificially low." Congress already noted that producers, who made profits on new gas in 1972 at $.26 per Mcf, suddenly in 1977 "required" $1.75 per Mcf before producing new gas.[140] When ERG states that anything less than a $3.224 per Mcf incentive price for old gas in 1982 is not a "commercially acceptable transaction," Appt's Br. 41, ERG's understanding of "acceptable profits" becomes clear.[141]

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[137] MacAvoy, *Price Formation in Natural Gas Fields*, 264 (1962).

[138] *Hearings on Implementation of Title I*, *supra* note 17, at 130 (statement of Dr. Cooper).

[139] Kansas Geological Society Library, Wichita, Kansas, *Drillers' Logs*, Kansas Producers.

[140] *Hearings on S.256*, *supra* note 17, at 43 (statement of Sen. Metzenbaum); 124 Cong. Rec. S14884 (daily ed. Sept. 11, 1978) (statement of Sen. Proxmire).

[141] Between 1978 and 1980, 82 oil and gas companies accounted for 96% of all increases in corporate net income in the Fortune 1000, a "transfer of wealth" that a House Committee found "alarming." *The Changing Distribution of Industrial Profits: The Oil and Gas Industry Within the Fortune 500, 1978-80*, H.R. Rep. No. 390, 97th Cong., 1st Sess. v, vi (1981).

The price that ERG demands as the "fair market value" of its old gas is the cartel-fixed OPEC equivalent price for natural gas,[142] an artificially *high* price established by Congress for the specific purpose of stimulating new production and exploration. Members of Congress commented that the price exceeded any freely competitive price for natural gas.[143] Indeed, the § 102 price is not even available for many *new* Kansas production wells, whether interstate or intrastate, which qualify under § 103 and not § 105. Barring ERG from receiving this price for its old natural gas is hardly the severe and unexpected impairment of ERG's contracts that ERG represents.

C. The Contract Clause of the United States Constitution Should Not Be Expanded to Prohibit State Participation in Formulating Energy Policy

The NGPA is premised on the idea that "[a] national energy plan can be built only on a foundation of partnership and understanding among the federal government [and] the states . . . which regulate or own a substantial part of United States energy resources." [144] After President Carter noted that "[m]any of the programs pro-

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[142] *See* H.R. Rep. No. 496, 95th Cong., 1st Sess. (pt. 4) 96 (1977). *reprinted in* [1978] U.S. Code Cong. & Ad. News 8549; H.R. Rep. No. 543, 95th Cong., 1st Sess. 44, *reprinted in* [1978] U.S. Code Cong. & Ad. News 7711-12. *See also* 124 Cong. Rec. H13418 (daily ed. Oct. 14, 1978) (statement of Rep. Dornan).

[143] 124 Cong. Rec. H13413 (daily ed. Oct. 14, 1978) (statement of Rep. Brown); 124 Cong. Rec. S14872 (daily ed. Sept. 11, 1978) (statement of Sen. Metzenbaum). *See Hearings on Deregulation, supra* note 17, at 27-28 (statement of R. Nader); *Hearings on Implementation of Title I, supra* note 17, at 326, 330-31 (statement of G. Lawrence); Federal Energy Regulatory Commission, *Notice of Inquiry: Impact of the NGPA on Current and Projected Natural Gas Markets, Docket No. RM82-26-000,* 47 Fed. Reg. 19157, 19160 (May 4, 1982).

[144] Executive Office of The President, Energy Policy and Planning, *The National Energy Plan* 89 (1977).

posed in the [National Energy] Plan cannot succeed without the active cooperation of state and local governments," [145] ERG seeks to impose serious constraints on the constitutional authority of the states to undertake their responsibilities in this national plan.

This Court has recognized that, notwithstanding the Contract Clause, states have a legitimate interest in experimenting with economic and social regulation.[146] "Courts and commentators frequently have recognized that the fifty states serve as laboratories for the development of new social, economic, and political ideas." [147] This experimentation is no less important when exercised within "the traditional authority of a State over resources within its boundaries which are essential not only to the well-being, but often to the very lives of its citizens." [148]

ERG is understandably concerned about future energy controls. Appt's Br. 39 n.53. The federal government has compelled states to consider energy regulations that may affect existing contracts,[149] and encouraged state regulation of market-distorting intrastate contractual provisions.[150] During national and state debates on natural gas pricing policy, with increasing "signs that the gas consuming public is approaching the limit of its willingness to accept higher and higher costs for gas," [151] ERG

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[145] *Id.*

[146] *See American Federation of Labor v. American Sash & Door Co.*, 335 U.S. 538, 547 (1949) (Frankfurter, J., concurring).

[147] *Federal Energy Regulatory Comm'n v. Mississippi* —— U.S. ——, 50 U.S.L.W. 4566, 4578 & nn.20-27 (June 1, 1982) (O'Connor, J., concurring in part and dissenting in part).

[148] *Sporhase v. Nebraska*, —— U.S. ——, 50 U.S.L.W. 5115, 5121 (July 2, 1982) (Rehnquist, J., dissenting).

[149] *See FERC v. Mississippi, supra* note 147.

[150] *See* NGPA §§ 105, 602; 15 U.S.C. §§ 3315, 3432 (Supp. IV 1980).

[151] *Hearings on Implementation of Title I, supra* note 17, at 370 (statement of E. Luntey).

seeks a constitutional barrier to state performance of these functions.

This Court has "emphatically refused to go back to the time when courts used the Due Process Clause 'to strike down state laws, regulatory of business and industry conditions, because they may be unwise, improvident, or out of harmony with a particular school of thought.' " [152] This Court has similarly refused to use the Contract Clause to reach that same end.[153] With the singular importance of energy to the welfare of state citizens, this is not an area in which strict new judicial scrutiny of legislative judgments is warranted. The Kansas Act satisfies the standards established by this Court in *Blaisdell* and *Allied Structural Steel* and should be upheld on that basis.

III. NGPA ESTABLISHMENT OF CEILING PRICES DID NOT "FIX A HIGHER PRICE" SUFFICIENT TO TRIGGER A PRICE INCREASE UNDER ERG'S GOVERNMENT PRICING CLAUSE

ERG alleges that the Court below misconstrued NGPA § 105(b) to "[freeze] the § 105(b)(1) price at the level of the November 9 contract price," and thus held that ERG's "government pricing" clause could not provide a price increase on December 1, 1978. Appt's Br. 44. The inherent contradiction in ERG's position reflects that the Court did not so hold.

NGPA § 105(b)(1) provides the ceiling for ERG's contracts, regardless of the escalation provision relied upon. Had the decision below held that § 105 freezes the contract price at the November 9, 1978, price, as ERG alleges, then no price escalation was possible under the

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[152] *Ferguson v. Skrupa*, 372 U.S. 726, 731-32 (1962).

[153] *Compare Marcus Brown Holding Co. v. Feldman*, 256 U.S. 170 (1921), *with Block v. Hirsh*, 256 U.S. 135 (1921). " 'The power of the state when otherwise justified' . . . is not diminished because a private contract may be affected." *East New York Sav. Bank v. Hahn*, 326 U.S. 230, 233 (1945) (quoting *Marcus Brown, supra*).

price redetermination clause in these contracts. ERG concedes, however, that the "ruling on Section 105(b)(1)" applies only to the government pricing clause, and "not to the wholly independent price redetermination clause." Appt's Br. 18 n.22. ERG thus admits that the decision does not interpret § 105 to freeze contract prices. The decision holds instead that ERG's government pricing clause, in conjunction with NGPA enactment, does not trigger a price increase.

This Court need not reach this question. This Court affirms judgments, and not the language of lower court decisions.[154] As ERG concedes, Appt's Br. 19 n.22, the Kansas Act limits, to the NGPA § 109 price, price increases under *both* escalator clauses. ERG filed this action for a declaratory judgment that it terminated its contracts, either pursuant to their terms in July 1979, after KPL refused to pay the § 102 price, or in August 1979 because of KPL's alleged breach in refusing to redetermine to that price The Act thus equally barred any contract right to terminate as well as the claim of breach. Constitutional application of the Act thus requires affirmance of the judgment. Whether ERG's government pricing clause may trigger a price increase in addition to that triggered by the redetermination clause is not significant.

The question herein is not, as ERG contends, whether NGPA § 105 prohibits the operation of ERG's government pricing clause, but whether the "mere establishment of the ceiling prices under this Act [NGPA] shall trigger indefinite price escalator clauses in existing intrastate contracts."[155] Contrary to ERG's contention, the Court below did not find that ERG's government pricing clause contractually triggered a price increase. KPL argued that

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[154] *See Schweiker v. Hogan*, —— U.S. ——, 50 U.S.L.W. 4750, 4754 (June 21, 1982).

[155] H.R. Rep. No. 1752, *supra* note 46, at 83.

ERG's clause only contemplated price increases to cost-based rates, and not to escalating incentive prices during phased deregulation. The Court disagreed, however, and held that "enactments *such as* the NGPA" would be sufficient to trigger the government pricing clause. J.S. App. 14a (emphasis added). The Court then examined the separate question of whether ERG's clause in fact triggered a price increase in conjunction with the NGPA.

The decision below must be read in light of the clarifying opinion on the same point in the *Mesa Petroleum* cases, issued on the same day.[156] The Court acknowledged, in conformity with *Pennzoil Co. v. FERC*, *supra*, 645 F.2d 360, that § 105 did not prohibit the operation of indefinite price escalator clauses, but neither did it require their operation. NGPA ceiling prices are available only if a contract otherwise so provides.

In contrast with all other NGPA Title I ceiling prices, § 105(b)(1) establishes as the ceiling price for intrastate gas, not a specific higher ceiling price, but the *lower* of the § 102 price and "the price under the terms of the contract." ERG claims that Congressional enactment of this provision "fixed a *higher* price" that triggered its government pricing clause up to the § 102 price. Nothing in § 105, however, establishes any higher price. ERG reads § 105(b)(1) as though it unqualifiedly fixed the § 102 price as the specific price ceiling. Had Congress so intended, it would have drafted § 105(b)(1) as it did § 102.

ERG claims that, under NGPA § 105, its contract price escalates to the § 102 price because the "price under the terms" of its contracts "by definition was and always will be equal to the maximum lawful price under

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[156] *Mesa Petroleum Co. v. KPL*, 229 Kan. 631, 629 P.2d 190, *clarified*, 230 Kan. 166, 630 P.2d 1129 (1981), *cert. denied*, 50 U.S.L.W. 3592 (Jan. 25, 1982).

§ 102." J.S. 26. ERG may therefore claim the § 102 price as the "lower" of the two prices set forth in § 105. ERG's "price under the terms" is a § 102 price, however, only *if* the clause has already escalated the contract price to the § 102 price. The circularity is obvious. ERG may only establish escalation based on that same claim of escalation. ERG cannot establish that § 105 triggers any escalation in the first instance.

Congress purposefully refused to prescribe a higher price for old intrastate gas. Congress announced its intention that "government pricing" type clauses in intrastate contracts would not function upon NGPA enactment. When escalator clauses are triggered by "just and reasonable rates" fixed by FERC, the "mere establishment of the ceiling prices under [the NGPA]" shall *not* trigger these clauses "in existing intrastate contracts." This comports with the NGPA policy that intrastate gas "not considered 'new' would get a lower price" than new intrastate gas under § 102.[157] NGPA intrastate pricing provisions preserved the status quo while reserving the issue of intrastate pricing to the states. Congress *permitted* escalator clauses for old intrastate gas to function according to their terms, based on prices being paid in the market, up to the § 102 price. Congress, however, did not *prescribe* the § 102 price as the ceiling, as it did for new gas. Indeed, this "prescribed price" for old gas would curiously be *higher* than the *new* production incentive price established for qualifying *new* intrastate wells under § 103.

The Fifth Circuit in *Pennzoil* originally reached this same conclusion. The initial panel opinion noted in dicta that NGPA § 105 permits the operation of both fixed price escalator clauses, which designate specific prices as "terms of the contract," and favored nation and rede-

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[157] 124 Cong. Rec. S14880 (daily ed. Sept. 11, 1978) (statement of Sen. Hansen).

termination clauses, which designate as the "terms of the contract" specific prices under other contracts. A government pricing clause, however, can look for its higher price only in the applicable statutory section—here § 105(b)(1).

> Some foresighted intrastate producers included legislative rate clauses in their contracts against the day Congress extended Federal price controls to the intrastate market. This clause will not escalate the Section 105(b)(1) contract's price to the Section 102 price. The maximum lawful § 105(b)(1) price is the lower of the current contract price or the Section 102 price. Absent some other escalation mechanism or ability to qualify under some other price and category, the current unescalated price is the maximum lawful price. In other words, the escalation provision is, in effect, looking to itself, and cannot be used to bootstrap the price any higher. The legislative rate clause, however, would suffice for collection of the maximum lawful price of some other category if the gas under the contract qualified for that category.[158]

ERG may not claim that "since the NGPA sets regulated prices higher than the contract price, the price under these contracts escalated . . . to the 'regulated price'" established by the NGPA. Appt's Br. 42. The "regulated price" established by the NGPA is not a higher price. Nor may ERG claim that its government pricing clause triggered an increase based on other NGPA prices for which the gas does not qualify. NGPA § 101(b)(9)

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[158] *Pennzoil Co. v. FERC*, No. 79-1247, slip op. at 7355-56 n.32 (5th Cir. May 20, 1981), *modified*, 645 F.2d 360 (1981). Phillips Petroleum, another Spivey producer with a contract like ERG's, petitioned the Fifth Circuit for rehearing and urged the Court to withdraw this language as dicta that might influence litigation between KPL and ERG. The Court denied the motion for rehearing, but withdrew this language from its footnote, although the Court issued no contradictory statement. The soundness of the unanimous panel's reasoning still stands.

provides that, if a contract establishes a price that *exceeds* the price under the applicable statutory section, then that applicable ceiling—here § 105—"supercedes and nullifies" the effectiveness of the contract price. 15 U.S.C. § 3311(b)(9)(A).

Congress expressly intended that establishment of NGPA ceiling prices would *not* trigger price increases under indefinite escalator clauses in intrastate contracts; ERG seeks precisely the opposite. ERG's entire argument ignores the language of the Conference Report and the structure of § 105(b)(1). The Court below correctly held that this escalator clause did not provide a price increase, and thus a contract right to terminate, that the Kansas Act forbids.

CONCLUSION

For the foregoing reasons, this Court should affirm the decision of the Kansas Supreme Court.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER & LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

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REPLY BRIEF FOR APPELLANT

In our opening brief, we showed that under this Court's precedents, state legislation violates the Contract Clause when it works a substantial impairment of contractual obligations, does not address an important general social problem, and is not a necessary and a reasonable means to achieve the statute's ostensible purpose. Appellee does not dispute this analysis, but instead undertakes, along with its chorus of supporting *amici*, to convince this Court that the Kansas Price Protection Act satisfies the Contract Clause test enunciated by this Court. We respond here only to their salient misconceptions.

I. KPL CANNOT MAKE THE IMPAIRMENT VANISH

A. *Reliance.* In our opening brief, we showed that abrogation of the indefinite escalator clauses at issue constitutes a substantial contractual impairment because the clauses were "the primary consideration for" ERG's agreement to guarantee to KPL its long-term supply of natural gas, and ERG "was substantially induced to enter into these contracts on the basis of" KPL's promise to pay the contract price, as adjusted according to the escalator provisions, or to permit ERG to terminate the contracts. *City of El Paso* v. *Simmons*, 379 U.S. 497, 514 (1965). KPL now disputes this contention, claiming that at the time of contracting ERG received a price for the gas at issue that was much higher than the market price; that neither ERG nor KPL ever anticipated that the indefinite escalator clauses would lead to prices as high as those authorized by the NGPA; and that ERG is therefore seeking the benefit of a "windfall" in demanding the price to which it is entitled under its contracts and § 105(b) of the NGPA. KPL Br. 3 & n. 9, 40-41.

KPL's self-serving contentions are impeached, however, by sworn testimony pertaining to these contracts (then being executed) given before the Kansas Corporation Commission ("KCC") on November 10, 1975, by Mr. John G. Williamson, then KPL's Executive Vice President. Tr. of Nov. 10, 1975, *In re Kansas Power & Light Co.* (KCC Dkt. No. 106,207-U).[1] In response to intensive questioning about the increase in the base contract price from $.19 to $1.53 per Mcf and the impact of the indefinite escalator clauses, Mr. Williamson explained that there was "much competition for the Spivey gas," such that the producers in question would "have no problem whatsoever marketing a package of gas such as is available out of Spivey" (R. App. 2a, 3a); that other prospective purchasers had offered the Spivey producers "just under $2.04 per Mcf at the wellhead" (R. App. 3a, 6a); that the "contracts for $2.04 were in evidence" (R. App. 5a); that the gas was "necessary to meet the demands of [KPL's] present customers" (R. App. 4a); that the contracts "certainly" were "the result of arm's length negotiation" that was "the longest and most complicated of anything we have ever been involved in" (R. App. 3a); that "[y]ou either provide an escalation or you don't buy gas these days" (R. App. 6a); that "[t]his is the case with any gas negotiations you are into" (R. App. 6a); that "you must provide escalation and you must provide price redetermination" (R. App. 6a); that "[t]here is no question in my mind but what the price of gas is going to go up wherever you are in the United States" (R. App. 8a); and that the inclusion of these escalator clauses as the *quid pro quo* for the "life of the field . . . dedication" of gas "is a distinct advantage to both parties in this situation and certainly one that was considered in the negotiations" (R. App. 9a).

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[1] Excerpts from Mr. Williamson's testimony are reproduced in an appendix to this reply brief, and will be cited herein as "R. App. ——." The full transcript has been lodged with the Clerk.

This testimony demonstrates beyond peradventure not only that KPL desperately needed the gas at issue to service its customers and that KPL recognized that the price of gas under the contracts was going to increase substantially,[2] but also that KPL was well aware that ERG had no reason to enter into long-term contracts with a base price of $1.53 per Mcf without the assurance that the price would escalate over the term of the contracts. Only after it managed to bind ERG to these long-term commitments did KPL lobby the Kansas legislature for the abrogation of the very escalator clauses and termination rights it offered ERG as the incentive to enter into the contracts. Under the Kansas statute, ERG is held to its delivery obligations but is stripped of the price that led it to make the commitment.[3]

B. *Future State Laws.* KPL further contends (at 22, 24, 39-40) that there has been no impairment of

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[2] Indeed, as we noted in our main brief (at 25 & n.35), Congress had before it, at the very time the contracts were executed, several gas deregulation proposals, the broadest of which was passed overwhelmingly by the Senate a month later. And, as the court below noted (J.S. App. 11a-12a), the government pricing clauses in the instant contracts—unlike those found in other producers' contracts—explicitly were intended to be triggered by a change in regulation effected by legislative action. Furthermore, while the Oklahoma Corporation Commission suggests that "had complete deregulation been established by Congress, ERG would have been stuck with the definite contract price, for there would have been *no* 'higher . . . regulated price'," OCC Br. 19-20 (emphasis in original), this simply is wrong. Whatever the effect would have been on ERG's *government pricing* clause, complete deregulation would have triggered escalation of the contract price under the *price redetermination* clause when higher prices were paid.

[3] The legislative history of the NGPA reflects, and KPL acknowledges (at 8 n.23), Congress' concern that in anticipation of deregulation "[g]as left in the ground [was] perceived as a better investment than cash in the bank." ERG did not withhold its gas; yet the Kansas statute nevertheless penalizes ERG for having made its gas available to Kansas consumers, and for having done so on a long-term basis.

ERG's contractual rights because the contracts by their own terms are "subject to all relevant future state and federal laws." According to KPL, ERG in effect agreed by this provision to be bound by any conceivable subsequent legislation, no matter how invalid, or at least not to make objection on Contract Clause grounds. As shown in our opening brief (at 25 n. 36), however, there is no such thing as an unconstitutional law that nevertheless can be considered a law.[4] Indeed, the "future state laws" provision does not change what would be true in its absence: All contracts are subject to applicable laws, including existing laws, amendments thereto, and subsequent legislation. "Not only are existing laws read into contracts in order to fix obligations as between the parties, but the reservation of essential attributes of sovereign power is also read into contracts as a postulate of the legal order." *Home Building & Loan Association* v.

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[4] Thus, we take issue with the conclusion of the court in *Edmiston* v. *State Corp. Comm'n*, No. 79-1335 (D. Kan. Nov. 24, 1980), *modified* (D. Kan. Jan. 13, 1981), *appeal docketed*, No. 81-1197 (10th Cir. Feb. 23, 1981), which in any event is contrary to the holding of the Kansas Supreme Court on the issue in the case at bar. See n. 6, *infra*. On September 13, 1982, the Tenth Circuit ordered further proceedings in *Edmiston* held in abeyance pending resolution of the instant case.

KPL's reliance on *White* v. *United States*, 270 U.S. 175 (1926), is wholly inapposite. There the subsequent legislation allowed the contracting party's intentions to be carried out better than had the original legislation. Also inapposite are the cases cited (at 18 & nn. 37 and 38) by *amicus* Oklahoma Corporation Commission. In each of those cases, the contract made specific provision for the contingency of specific legislative action, and in each case the specific event provided for in the contract came to pass. As the court said in *National Bldg.* v. *State Bd. of Educ.*, 510 P.2d 510, 512 (N.M. 1973), "Thus by its very terms, the lease contemplates exactly what came to pass: . . . [the state legislation] merely fulfilled one of the terms expressly contracted for by the parties." The "future . . . laws" clause, on the other hand, did not anticipate a specific contingency and cannot be construed as a blanket waiver by ERG of its constitutional rights.

Blaisdell, 290 U.S. 398, 435 (1934).[5] Laws enacted pursuant to this power nevertheless are subject to challenge and invalidation under the Contract Clause; it is a question of "harmonizing the constitutional prohibition with the necessary residuum of state power." *Id.* KPL therefore begs the question by claiming that the "future . . . laws" clause settles this dispute.[6]

II. THE KANSAS STATUTE IS NEITHER REASONABLE NOR NECESSARY

A. *NGPA Pricing Policy.* There is perhaps no more misleading argument advanced by KPL and its supporting *amici* than their portrayal of the NGPA as a statute that draws a bright line between all "new" gas, worthy of higher prices as an incentive for development, and, on the other hand, all "old" gas, whether previously regulated in the interstate market or previously free of controls in the intrastate market. On the basis of this incorrect premise, KPL (at 1-2, 5, 9-13) argues (a) that the Kansas Price Protection Act's use of the low NGPA § 109 price as a ceiling on price increases triggered by indefinite escalator clauses for the gas at issue here is consistent with the NGPA, and therefore presumably "reasonable" within the meaning of the Contract Clause,

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[5] See also *Union Dry Goods Co.* v. *Georgia Pub. Serv. Corp.*, 248 U.S. 372, 376 (1919): " 'Contracts must be understood as made in reference to the possible exercise of the *rightful* authority of the Government . . . .' " (citation omitted) (emphasis added).

[6] In any event, KPL's argument pertaining to the meaning of this provision is precluded in this Court by the decisions of the Kansas courts below. By reaching and deciding the federal constitutional question of the Kansas statute's validity under this Court's precedents, the Kansas courts necessarily rejected KPL's argument—which KPL also made below—that there is no impairment because the contracts by their terms incorporate any and all future laws whether or not such laws are valid. This Court therefore need not concern itself with the state law issue of the meaning of this contract provision. See, *e.g.*, *Fry Roofing Co.* v. *Wood*, 344 U.S. 157, 160 (1952); *Grayson* v. *Harris*, 267 U.S. 352, 357-58 (1925); *Portland Ry., Light & Power Co.* v. *Railroad Comm'n*, 229 U.S. 397, 412 (1913).

and (b) that ERG is not legitimately entitled to a "windfall" price in excess of the § 109 ceiling. KPL's premise, however, is wrong: The NGPA draws finer and more carefully considered distinctions in its pricing mechanisms for gas not qualifying as "new", and does not treat all previously discovered gas—to which KPL refers as "old", an adjective never used in the statute—as the black sheep of the natural gas family.

The NGPA specifically mandates that some previously discovered gas—namely, intrastate gas subject to an existing contract as of November 8, 1978, like that at issue here—be treated specially. A separate section of the statute—§ 105(b)—governs such gas. It is undisputed that § 105(b)(1) allows the price of "old" intrastate gas to rise according to the terms of the contract to which it is subject, up to the ceiling for new gas set by § 102. As one can easily glean from the appendix to our main brief, the § 102 ceiling is substantially higher than the § 109 ceiling. The whole purpose of § 105 is to allow the continued operation of intrastate contracts in existence before the enactment of the NGPA. Subject to the limitations imposed by § 105, it was Congress' intention that "[i]ntrastate contracts in existence on the day of enactment of [the NGPA] shall be *sanctified.*" *Staff of the House Comm. on Interstate and Foreign Commerce and the Senate Comm. on Energy and Natural Resources, 95th Cong., 2d Sess., Natural Gas Pricing Agreement Adopted by the Conferees on H.R. 5289,* at 18 (Comm. Print 1978) (emphasis added). Congress obviously understood and intended that some "old" intrastate gas would earn the § 102 price.

KPL supports its distorted reading of the NGPA with a misleading use of legislative history. Most of the cited material (see KPL Br. 5 & n. 14, 6-7, 8 & nn. 23 & 24, 9 & n. 27, 10 & nn. 28-30, 11 & n. 34, 13 & nn. 43 & 44) was prepared in connection with the Carter Administration's proposed legislation, which was passed by the

House in 1977. That bill would have placed ceilings lower than those contained in the NGPA on intrastate as well as interstate gas. The Senate, however, took a radically different approach. The Pearson-Bentsen amendment in the Senate would have left the intrastate market wholly free of controls and deregulated the interstate market, too, on a speedier timetable than that eventually set out in the NGPA. "The difference in projected economic impact between the House and Senate bills was enormous." Ligon, *Problems of Contractual Authorization to Collect NGPA Wellhead Prices*, 57 Tex. L. Rev. 551, 552 (1979).

The NGPA itself emerged as a compromise measure, intended, in the words of the Conference Committee Report, to "reconcile[] these two very different bills." H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 68 (1978). It placed ceilings on both interstate and intrastate gas, but set them high enough to encourage exploration and new production. More important for purposes of this case, the conferees sought to protect previously existing contract rights, recognizing an equity independent of the encouragement of new production. See p. 6, *supra*. Indeed, the conferees even were willing to abide prices for "old" intrastate gas in *excess* of the NGPA new gas price: § 105(b)(2) permits the collection of previously existing contract prices for "old" intrastate gas even if they exceed the § 102 incentive price.

It is, therefore, incorrect and misleading to state that the NGPA allows "higher prices *only* for certain categories of natural gas where increased production and supplies might result." KPL Br. 5 (emphasis added). It is in connection with "old" *interstate* gas that Congress intended, and § 104 of the NGPA provides, for consistently lower prices. The reason is as fair as it is simple: higher prices for such gas would neither honor existing contract rights nor generally foster exploration and increased production, since lower prices for such gas already were set according to the cost-based approach

mandated by the Natural Gas Act.[7] Section 109 follows suit by using the highest § 104 price for, *inter alia*, "old" intrastate gas *not* subject to contract as of the date of enactment of the NGPA, as to which there could be no reliance interests. But in order to fulfill its goal of accommodating existing contracts rights, Congress rejected the kind of rigid, simplistic approach now imputed to it by KPL, and instead included § 105 in the statute, specifically contemplating that some producers like ERG will, by virtue of their contracts rights, receive the § 102 price for gas such as that at issue here.

B. *Kansas Pricing Policy.* Even if KPL were correct in describing the NGPA as distinguishing simplistically between "new" gas and gas already discovered, the Kansas Price Protection Act does not comport with this format. While the Kansas statute restricts indefinite escalator clauses for "old" gas under contract as of April 20, 1977, it allows increases—all the way up to the § 102 price—called for by indefinite escalator clauses in contracts executed after April 20, 1977, even though indefinite escalator clauses were at least as prevalent after that date as before. See ERG Br. 31 n. 43. If the Kansas legislature intended to provide "incentive" prices only in connection with the development of new gas, there is no rational justification for it to have allowed contracts executed after April 20, 1977 and covering gas already discovered to rise to the § 102 price.[8]

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[7] Thus, to the extent that anyone considering the Carter Administration's proposed legislation in 1977 thought "it would be a silly political idea to *deregulate* old gas," see KPL Br. 13 (emphasis added), they had in mind old *interstate* gas, which already was subject to price controls, but not old intrastate gas already subject to contract, which was not.

[8] KPL offers no defense of the Kansas statute's exemption of contracts executed on or after April 20, 1977. *Amici* Oklahoma Natural Gas *et al.* ("ONG") suggest (at 22) that the exemption is reasonable because "President Carter announced his proposed new energy policy" on that date, such that producers "might be thought

Moreover, the Price Protection Act certainly does not conform to the NGPA insofar as its voluntary renegotiation provision, K.S.A. § 55-1408, allows natural gas purchasers to dictate under what circumstances gas producers may obtain prices higher than those authorized by the Act. Indeed, we know of no other price control legislation (besides the Oklahoma legislation from which the Kansas statute was copied) that delegates to a private party the right to decide when the controls may be set aside. Neither KPL nor any of the *amici* has offered any justification for providing KPL with this license to bargain away for its own benefit the very consumer interests that are claimed to be the justification for the legislation.

C. *Section 602.* KPL (at 1, 10, 15) argues that § 602(a) of the federal statute provides "express authorization" for the Kansas statute's abrogation of pre-April 20, 1977 indefinite escalator clauses and associated contract termination rights. Section 602(a), however, merely provides that the NGPA does not preempt the power of states to "establish or enforce any maximum lawful price for the first sale of natural gas produced in [the] State" not exceeding applicable NGPA ceilings. While certain of the *amici* cite legislative history to the

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to have had expectations of sharply higher prices after that date." As we observed in our Reply to Appellee's Motion to Dismiss (at 3 n.5), there is no basis in the Kansas legislative history for this *post hoc* rationalization, and it hardly seems fair to penalize producers who foresaw in 1975—when deregulation legislation easily had passed the Senate—that higher prices were forthcoming, see pp. 2-3 & n. 2, *supra*, while rewarding producers who made the same judgment in 1977. Apparently recognizing the weakness of their first argument, *amici* ONG also observe (at 22), without further argument or explanation, that "[t]he same date of April 20, 1977 is used as the base date for pricing purposes throughout the NGPA." But the date is used in the two sections of the NGPA cited by the *amici* in connection with categorizing gas on the basis of when it was first produced from a well, not on the basis of when contracts for the gas were executed. There is thus no correlation between the use of the date in the federal and state statutes.

effect that under § 602(a) the states have authority to regulate indefinite escalator clauses, see KCC Br. 23; ONG Br. 9-10, the Federal Energy Regulatory Commission ("FERC"), after reviewing the same legislative history, has agreed with our construction of these materials (at 34-35 n.49). FERC has ruled that under § 602(a) Congress merely ceded to the states "the authority to further limit the operation of price escalator clauses *as an adjunct* to their authority to prescribe lower maximum lawful prices . . . within the state." 44 Fed. Reg. 16895, 16898 (March 20, 1979) (emphasis added). Thus, according to this virtually dispositive construction of § 602(a) by the agency charged with enforcing the NGPA, see, *e.g.*, *FEC* v. *Democratic Senatorial Campaign Committee*, 454 U.S. 27, 39 (1981), a state may prohibit prices in excess of fixed ceilings and then "supplement[]" that ban "by prohibiting price increases that exceed the [ceilings], if the increases are the products of certain varieties of contractual price escalation clauses." *Permian Basin Area Rate Cases*, 390 U.S. 747, 781-82 (1968). This kind of general natural gas price legislation is a far cry from the actions of Kansas and Oklahoma, where prices have no limit *unless* they result from the operation of an indefinite escalator clause.

But even if FERC is wrong (and KPL and its *amici* are right) about the congressional purposes underlying § 602(a), this Court has made it abundantly clear, as we have shown in our opening brief (at 34-35), that Congress cannot invite States to pass laws violative of the United States Constitution by enacting a non-preemption provision such as § 602(a). See, *e.g.*, *New England Power Co.* v. *New Hampshire*, 50 U.S.L.W. 4223, 4225-4227 (U.S. Feb. 24, 1982). If the state legislation violates the Contract Clause test enunciated by this Court in *Blaisdell* and its recent progeny, it is unconstitutional, and Congress could have neither the intention nor the power to change that result.

D. *Pass-Throughs.* KPL does not contest that the Kansas statute would violate the Contract Clause if, "without modifying the [contract] at all, [Kansas] could have adopted alternative means of achieving [its] goal[]." *United States Trust Co.* v. *New Jersey*, 431 U.S. 1, 29-30 (1977); see *City of El Paso, supra*, 379 U.S. at 516-17.[9] We have shown (at 31-32, 37) that the KCC or the Kansas legislature could have denied a pass-through of all or part of KPL's increased costs, thereby providing a "modicum of restraint on some utility price increases," J.S. App. 75a, without diluting ERG's contract rights.

KPL does not question the KCC's general authority to exclude imprudently incurred costs in determining whether KPL's rates are just and reasonable.[10] Nevertheless, KPL (at 4-5, 27) and the KCC (at 15) now contend for the first time in this litigation that the KCC's approval in April, 1977, of a so-called "purchased gas adjustment clause" ("PGA clause") entitles a utility to "the immediate pass-through to consumers of all in-

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[9] The KCC erroneously argues (at 18-19) that a more lenient standard of review than that set forth in *United States Trust* is appropriate where, as here, the state legislation does not affect a contract to which the state is a party. This Court made clear, however, in *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234, 247 (1978), that the test articulated in *United States Trust* is equally applicable in cases involving private contracts. See ERG Br. 37 n.51.

[10] *Amici* ONG argue (at 24 n.36), however, that "it is not the function of rate-making authorities to second-guess the decisions of management" and that "regulatory bodies must ordinarily base their decisions on the utility's actual operating expenses" so long as those expenses resulted from an arms-length transaction. It is, however, by no means rare in ratemaking for regulatory commissions to disallow actually incurred operating expenses as unreasonable or excessive. See, *e.g.*, *Metropolitan Edison Co.* v. *Pennsylvania Pub. Util. Comm'n*, 437 A.2d 76, 80 (Pa. Commw. Ct. 1981); *Boise Water Corp.* v. *Idaho Pub. Util. Comm'n*, 555 P.2d 163, 171 (Idaho 1976); *City of Evansville* v. *Southern Ind. Gas & Elec. Co.*, 339 N.E.2d 562, 569 (Ind. Ct. App. 1975); *Colorado Mun. League* v. *Pub. Util. Comm'n*, 473 P.2d 960, 967 (Colo. 1970).

creased costs for natural gas." Their prior omission of this argument is understandable.

In authorizing the PGA, the KCC did not divest itself of the authority to deny a pass-through if it would result in rates that would not be "just and reasonable." K.S.A. §§ 66-107, 66-110.[11] Indeed, KPL has expressly acknowledged that the PGA clause does not guarantee an automatic pass-through.[12] And even if the KCC's order au-

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[11] The KCC stated expressly that its "energy cost adjustment clause must be coupled with specific reporting requirements and effective monitoring procedures to insure that only legitimate energy costs are included in the adjustment." *In re General Investigation To Establish General Policies With Regard To Purchased Natural Gas* 13 (Kan. Corp. Comm'n, Dkt. No. 106,850-U, Order of April 19, 1977). In this connection the KCC has required each natural gas utility to "provide to the Commission a statement of the justification for every escalation invoked under the terms of its existing contracts." *Id.* 24.

Similarly, other states that have authorized PGA clauses have made clear that they retain the power, notwithstanding any such clause in a utility's tariff, to assess the reasonableness of energy cost increases to be passed through to the ratepayers. For example, in a case strikingly similar to this one, the Commonwealth Court of Pennsylvania recently upheld the decision of that state's Public Utility Commission refusing to allow a pass-through of certain fuel costs under a utility's fuel adjustment clause, because the utility had imprudently renegotiated coal contracts to provide for higher prices in the wake of the sudden general escalation of fuel prices following the oil crisis of 1973. *Metropolitan Edison Co., supra,* 437 A.2d at 76. The court expressly rejected the utility's argument that the Commission improperly substituted its judgment for that of management. *Id.* at 80.

[12] In May 1979, shortly after enactment of the Kansas Price Protection Act, KPL's then Executive Vice President, John G. Williamson, testified before the KCC as follows:

> "Q. Can the Commission suspend the operation of [the] PGA on any one of [KPL's] filings?
>
> A. Yes. They have the right to oversee what we are doing, looking at contracts and things of this sort." Transcript of May 2, 1979, at 18-19. *In re Kansas Power & Light Co.* (Kan. Corp. Comm'n Dkt. No. 118,447-U).

thorizing the inclusion of a PGA clause in utility tariffs were construed to prevent the KCC from *suspending* the pass-through of purchased-gas costs deemed unreasonable by the Commission, Kansas law empowers the KCC to examine the propriety of those costs by initiating an investigation of the utility's rates. K.S.A. § 66-110.[13] Finally, whatever the meaning and effect of the PGA clause, neither KPL nor the *amici* have adequately responded to our contention (at 37) that instead of creating a false dichotomy between producers and consumers, the Kansas legislature could have asserted its own authority to prohibit all or part of the pass-through of increased costs to consumers.

KPL asserts (at 38) that it could not be made to bear the burden of increased gas costs. If KPL means to rely on constitutional restrictions on state regulation of utility rates, see ONG Br. 24, that reliance is misplaced. Such cases as *FPC* v. *Natural Gas Pipeline Co.*, 315 U.S. 575, 585-86 (1942), give broad latitude to regulatory authorities, and KPL has made no showing that Kansas would exceed that latitude by imposing all or part of the increased costs on KPL. Indeed, since the Price Protection Act reaches only a portion of cost increases caused by indefinite escalator clauses and pro-

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[13] State utility commissions have routinely protected consumers from unreasonably high costs by, *inter alia*, adjusting the utility's allowed rate of return in a way that cushions consumers from unwarranted price increases. See, *e.g.*, *Re Virginia Elec. & Power Co.*, 44 PUR 4th 46, 50-51 (Va. Corp. Comm'n Aug. 24, 1981); *Re General Telephone Co. of Calif.*, 37 PUR 4th 127 (Calif. P.U.C. Oct. 22, 1980). KPL's PGA clause therefore at best affects the timing of the KCC's review of cost increases triggered by indefinite escalator clauses in KPL's contracts. That conclusion comports with general practice regarding such clauses. For example, FERC has recently ruled that it intends to examine carefully during its ratemaking proceedings any costs incurred pursuant to interstate PGA clauses with an eye toward forcing interstate pipelines eventually to bear increased costs associated with the purchase of high cost gas from producers. See Bureau of National Affairs, *Energy Users Report* 1013 (Oct. 7, 1982).

vides at best only a "modicum" of restraint in gas prices, KPL might very well be able to bear the entire burden. If, on the other hand, KPL means to imply that ERG could better afford the financial cost, there is nothing in the record or open to judicial notice that remotely supports such a conclusion, and ERG vigorously disputes any such contention.

E. *Incremental Pricing.* KPL observes that in May, 1980, the KCC by order implemented, in its rate design structures for Kansas utilities, " 'a form of incremental pricing consistent with the NGPA.' " KPL Br. 38 (quoting *Midwest Gas Users Association* v. *State Corp. Commission*, 623 P.2d 924, 927 (Kan. Ct. App. 1981)). As we have shown in our main brief (at 37-38), rules of this nature, which have been urged upon the states by FERC, pass on a utility's increased costs more rapidly to "low priority" users (primarily industrial concerns) which can better absorb them and substitute more economical fuel sources. The KCC's willingness to adopt such rules further undercuts the already limited justification for the legislation at issue, because with incremental pricing ordinary residential consumers would be cushioned from the impact of the increased fuel costs at issue—without any need to impair existing contracts. Instead of spreading the costs associated with KPL's contracting provisions across the Kansas industrial spectrum, the Kansas legislature has opted to place this burden on certain natural gas producers who agreed to guarantee KPL and its customers a long-term supply of gas.

F. *Termination.* It is also obvious that the legislature could have followed the simplest and fairest course of allowing termination of contracts containing the disfavored clauses, especially if those contracts, like ERG's, specifically provide for termination in the event that the seller cannot collect the escalated price called for by the contract. In the *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), this Court sustained the constitution-

ality of the FPC's regulation of natural gas prices by relying in part on the fact that parties affected by the regulation could abandon their activities or seek relief from the FPC rather than comply with the FPC's price controls. See *id.* at 770, 772. Kansas has not provided such an escape valve. It is one thing to set a ceiling on the purchase price of a commodity; it is quite another to require a producer to sell his goods at that price against his will, especially when he and the purchaser agreed to something entirely different.[14]

III. THE KANSAS STATUTE DOES NOT ADDRESS AN IMPORTANT GENERAL SOCIAL PROBLEM

A. *The Statute's Limited Reach.* KPL acknowledges (at 36) that only ten percent of the gas consumed in Kansas is covered by contracts that include indefinite escalator clauses. It fails to acknowledge, however, that because of its exemptions, the Price Protection Act addresses only a fraction of the gas covered by these contracts. ERG Br. 10-11, 30-31. Given the limited reach of the legislation, the protections which could otherwise be afforded consumers by the KCC by incremental pricing, and the Kansas legislature's own admission that the legislation only "would provide a *modicum* of restraint on *some* utility price increases," J.S. App. 75a, we fail to perceive the way in which the legislation solves "an important general social problem," *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234, 247 (1978), or in which "the vital interests" of Kansas would be served by it. *Blaisdell*, 290 U.S. at 434.

B. *Purposes of the Contract Clause.* KPL contends (at 31-32) that, even if the Act provides only a "modicum" of protection to residential consumers, this is a legitimate legislative goal which justifies the severe

[14] If the § 102 price is "artificially high," as KPL claims (at 7, 18, 42), then it should be able to buy cheaper substitutes for its terminated commitment from ERG, and the result will not be, as KPL threatens (at 38), that "Kansas citizens [will have to] survive without natural gas."

abridgement of ERG's contractual expectations.[15] KPL has lost sight of the fact that the Clause was included in the Constitution to prohibit very similar state legislation. After the Revolution, there was "an entirely inadequate supply of money of fixed and known value," B. Wright, *The Contract Clause of the Constitution* 6 (1938), not unlike the situation with regard to energy today. Many states responded in part by passing legislation staying or postponing the payment of private debts beyond the time fixed in contracts, or allowing debtors to pay their debts in depreciated currency, or in commodities, or in several installments over months or years. *Id.* 4. The debtors were numerous and considered deserving of relief, or else the state legislatures would not have responded as they did. *Id.* 6.[16]

Nevertheless, the Framers concluded that this kind of legislation was short-sighted and "contrary . . . to every principle of sound legislation," and that it was more important in the long run, and more in conformity with "the genuine sentiments [and] the undoubted interests" of the American people, to prohibit such state legislation. *The Federalist*, No. 44, at 301 (J. Cooke ed. 1961).

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[15] While KPL contends that the statute provides important relief to "the poor," there were no figures presented to either the Kansas legislature or the Kansas courts demonstrating the degree to which benefitted consumers are impoverished; even *amicus* Kansas Legal Services Corporation acknowledges (at 17) that "no data are available on the impact on high energy costs on low income Kansans."

[16] As one of the leading scholars of the Contract Clause has written:

> "It is not necessary to ascribe disreputable motives to the state legislator who voted for the debtor relief laws. To many of them statutes of this kind must have seemed to present the smallest proportion of evils. If all debts were required to be paid precisely as set forth in the contracts it could but mean in that period, particularly in the years of economic depression immediately preceding the adoption of the Constitution, great and doubtless unwarranted hardships for many an honorable debtor." B. Wright, *The Contract Clause of the Constitution* 6 (1938).

To this end the Framers adopted the Contract Clause, as a "constitutional bulwark in favor of personal security and private rights." *Id.* Thus, while the Contract Clause must doubtless be applied flexibly when "vital interests" would be served, the purported justification for the Kansas Price Protection Act is not far from the historical situation that prompted the writing of the Contract Clause in the first place, and it therefore cannot prevail.[17]

C. *Special Legislation.* While *Blaisdell* and its progeny do not require that we show that the Kansas statute was enacted with the specific intent of assisting KPL, evidence of this fact casts doubt on the claim of an important general social purpose. In our main brief, we demonstrated (at 31-33) not only that the statute assisted KPL far more than Kansas consumers,[18] but also that

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[17] Citing *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), and *FPC* v. *Texaco, Inc.*, 377 U.S. 33 (1964), *amici* ONG argue (at 16-17) that "[r]egardless of whether the prior FPC actions and court decisions involved precisely the same legal issues as those presented here, they establish that indefinite price escalator clauses are a matter of legitimate public concern, so that state governments are acting within the proper scope of their police powers when they act to limit their effect." See also KPL Br. 29. This Court cannot simply disregard, however, that neither the Contract Clause nor state legislation was involved in *Permian Basin* or *FPC* v. *Texaco*; the Contract Clause was written to curb certain kinds of state legislation even though similar restrictions deliberately were not placed on the federal government. See B. Wright, *supra* note 16, at 116. Moreover, indefinite escalator clauses were "a matter of public concern" in those cases only to the extent they were inconsistent with the since rejected federal regulatory policy underlying the Natural Gas Act. Furthermore, as this Court's opinions make plain, these federal regulations were tailored to minimize or entirely prevent impairment of preexisting contract rights. ERG Br. 40 n.55; see pp. 10, 14-15, *supra*.

[18] In addition to the adverse consequences that would have been suffered by KPL even in the event of a pass-through of increased costs to its customers, KPL also would have been hurt if the legislature had passed the Price Protection Act but had permitted termination of these contracts, because KPL's $3.6 million investment in

there was widespread concern within the Kansas legislature that the legislation was principally designed to aid KPL in its contract disputes with its natural gas suppliers. KPL and the several Oklahoma *amici* reply that the Oklahoma legislature passed a nearly identical statute. But as was emphasized by the minority of the special committee that recommended passage of the Kansas bill, "there are substantial differences between the gas markets in the two states," J.S. App. 82a, and the asserted need for legislation of this sort was far greater in Oklahoma, where 65% of intrastate gas was subject to indefinite escalator clauses (as opposed to 37% in Kansas) and where the monetary savings were projected to be 15 times greater than in Kansas. *Id.* 82a-83a.[19] In any event, the Oklahoma statute is not directly at issue in this case, and that statute's constitutionality depends on the circumstances in which it arose[20] and which it addresses.[21]

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gathering and transmission facilities in the Spivey-Grabs field would have been rendered "useless." R. App. 1a, 4a-5a.

[19] We note that none of the other major gas-producing states, including the two largest (Texas and Louisiana), have enacted similar legislation. This fact undermines KPL's highly exaggerated claim that the cause of federalism will suffer substantially if the Kansas statute is struck down.

[20] It would be difficult to respond to *amicus* OCC's recitation (at 8-11) of the supposedly thorough consideration afforded the Oklahoma statute given that it is admittedly based on "the memory of the author of [the] brief." OCC Br. 9 n.25.

[21] *Amici* ONG (at 20) chastise ERG for pointing out that the Kansas Supreme Court's finding that the Kansas statute was a response to an "emergency situation" (J.S. App. 22a) is supported neither by the record nor the statute's legislative history. *Amici* ONG (at 20) argue that the Oklahoma statute from which the Kansas statute was copied contains a declaration of an emergency in Oklahoma. Leaving the differences between the Oklahoma and Kansas situations aside, this Court should be informed that a declaration of an emergency is routinely included in Oklahoma legislation because in the absence of such a declaration, the Oklahoma Constitution requires that legislation not take effect until 90 days

IV. THE KANSAS SUPREME COURT INCORRECTLY CONSTRUED SECTION 105(b) OF THE NGPA

We find KPL's argument pertaining to the Kansas Supreme Court's construction of § 105(b) to be too incomprehensible to permit a cogent reply. Instead, we respectfully refer the Court to our earlier explanation of the Kansas Supreme Court's error; that explanation incorporates arguments already advanced to this Court by the United States and FERC on the identical issue. See ERG Br. 42-48. We emphasize (a) that this case cannot be resolved without deciding this issue of statutory construction, see ERG Br. 32 n. 57; and (b) that the Kansas court's holding does not decide a purely state law question of contract interpretation, because "the sole basis for the court's view as to the insufficiency of the contract escalation mechanism was its erroneous reading of the federal statute." ERG Br. 47.[22]

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after the end of the legislative session. Constitution of Oklahoma, Art. 5, § 58. Thus, "in recent times the majority of bills passed have had emergency clauses." Oklahoma Legislative Council, *Oklahoma Legislative Manual* 33 (1978). During the 1979 legislative sessions in which the Oklahoma Price Protection Act was passed, declarations of an emergency were included in bills, *inter alia*, establishing a Board of Cosmetology, recreating the Will Rogers Memorial Commission, and making appropriations for the Okeene, Oklahoma Rattlesnake Hunt and the Jay, Oklahoma Huckleberry Festival.

[22] While we cannot make sense of most of KPL's argument concerning § 105(b), we can isolate two points that could be unnecessarily confusing to the Court if not addressed. First, KPL relies on certain language originally contained in the slip opinion in *Pennzoil Co. v. FERC*, 645 F.2d 360 (5th Cir. 1981), *cert. denied*, 102 S. Ct. 1000 (1982), which KPL acknowledges (at 48 & n.158) was withdrawn by the panel. It goes without saying that reliance on withdrawn language is without sound foundation; and it also is apparent that the language was withdrawn because the Fifth Circuit realized it was wrong. See 645 F.2d at 374-75.

Second, KPL cites the conferees' statement that they did "not intend that the mere establishment of the ceiling prices under [the NGPA] shall trigger indefinite price escalator clauses in existing

CONCLUSION

The judgment of the Kansas Supreme Court should be reversed.

Respectfully submitted,

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intrastate contracts." H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978). But the conferees' statement at most means that clauses like area rate clauses would not be triggered all the way to the NGPA ceilings unless sales at these ceiling prices actually were being made: "Once natural gas is sold pursuant to the ceiling prices under this Act, such clauses would be activated as limited by this section." *Id.* Since sales at the § 102 price were made as of the effective date of the NGPA, KPL's point is difficult to comprehend. Moreover, the Fifth Circuit has suggested that a government pricing clause like ERG's *was* intended by the conferees to be triggered by the mere establishment of ceiling prices under the NGPA, even if ERG's price redetermination clause would not be so triggered. See *Pennzoil*, 645 F.2d at 378.

APPENDIX

Excerpts from Transcript of Testimony taken before the Kansas Corporation Commission, November 10, 1975 (Docket No. 106,207-U).

JOHN G. WILLIAMSON

being first duly sworn to testify the truth, the whole truth, and nothing but the truth, testified on his oath as follows:

DIRECT EXAMINATION

BY MR. GRIMES (for the Kansas Power & Light Co.):

* * * * *

[13] Q Mr. Williamson, what precipitated the filing of the application you have just identified?

A Well, Kansas Power and Light Company has been purchasing gas in the Spivey-Grabs Field since early 1956 under contracts that were negotiated with quite a large number of producers. Those contracts were so written that they would expire at the end of this year, December 27, 1975, or would terminate certainly unless the producers saw fit to let them ride through.

* * * * *

[18] Q I believe you indicated that your involvement in Spivey-Grabs [19] started in 1950 or thereabouts. Is that correct?

A Early 1956, yes, sir.

Q What is your company's gross investment in the Spivey-Grabs Field in order to take gas from it at this time?

A Our gross investment in the field is about $3,600,000. This includes the investment in the gathering system, the measurement facilities, the horsepower in the compressor station, and a transmission line that moves from the Spivey Field to our main transmission

system just north of there at our Calista compressor station.

* * * * *

[25] Q Now, Mr. Williamson, with reference to your so-called old contracts, or those that are expiring December 27, 1975, what were the prices under those contracts?

A At the present time, the prices under those contracts are 19 cents per Mcf for both gas streams.

* * * * *

Q When did your efforts to extend these contracts beyond December of 1975 commence?

A Actually, the first attempt of getting underway on this I believe was made in about July of 1973, and then as we [26] moved along we became more involved in the negotiations, and probably in about December of that year we got more specifically involved in them.

Q Are the volumes that you have been taking from Spivey significant in your total requirements?

A Very much so. Last year they were approximately 17 to 18 percent of our total purchases.

Q Have there been, to your knowledge, other bidders or seekers of this gas that you have been attempting to contract for since 1973?

A We have certainly been so advised, that there has been much competition for the Spivey gas.

Q Are your efforts to acquire gas in Spivey continuing at this point in time?

A Yes, in that we are continuing now working with those producers who have not signed the contracts, of course, urging them to do so, and we have had some contacts from them. I am sure, from their standpoint, they are interested in the outcome of these particular proceedings.

Q Do you know of other prospective purchasers for the gas that you have been negotiating for?

A Well, certainly the City of Wichita, or the WI.E.C., [27] has been a prospective purchaser. There is also

Anadarko Production Company. We have heard of an industrial company, a [sic] industry outside the state, who is interested in the gas, and at one time we heard that there was a fertilizer company that was interested in the possibility of purchasing Spivey gas.

Q Based upon your general familiarity with gas production and gas buying and selling, do you have any question in your mind as to whether or not the producers of this gas can market it to somebody other than KPL?

A They will have no problem whatsoever marketing a package of gas such as is available out of Spivey.

Q Were the negotiations that you mentioned starting in 1973 long and complicated?

A Well, I would certainly have to say that from my standpoint and from our company's standpoint, they were the longest and the most complicated of anything we have ever been involved in, ce tainly. There were many meetings, many telephone calls, much correspondence, a lot of travel, and a lot of hours were spent on the part of both the producers and KPL.

* * * * *

[28] Q Were the contracts marked as Exhibits 1-A and 1-B the result of arm's length negotiation?

A They certainly were, yes.

* * * * *

[32] Q Mr. Williamson, do you have any knowledge as to the price paid by W.I.E.C. for the gas volumes they have contracted for in Spivey?

A It is my understanding that W.I.E.C. has offered $1.85 per Mcf based on 1,000 BTU gas at the wellhead, with a maximum BTU consideration of 1100, which would take the price to just under $2.04 per Mcf at the wellhead.

Q Has that had an impact on your negotiations?

A Well, I am quite certain that it has because that price came into being as we were in negotiations and

I am quite sure that this must have had quite a lot to do with the thinking of the producers and the price that KPL should pay for their gas.

Q Had the Wichita contracts been executed before the conclusion of your negotiations?

A Yes, sir, they had.

Q Mr. Williamson, are the volumes of gas that you have been getting from Spivey and you hope to get in the future necessary to meet the demands of your present customers?

A Yes, sir, they are.

* * * * *

[43] Q Mr. Williamson, do the contracts attached as Exhibits A and B have a so-called upset date on them?

A Yes. They have an upset date of November 15.

Q Have any of the producers shared with you their intentions in the event this application has not been considered and favorably decided by that date?

A Yes, they have. They have certainly indicated to me that their desire is to see this hearing resolved properly and quickly. We have been negotiating for some long period of time over this. As a part of those negotiations it certainly was our understanding with them that if we were successful in being able to bring negotiations to a conclusion as soon as possible, that we would make a filing such as we have done with the KCC in the hope that the KCC would see fit to let us put the new prices into effect as soon as possible, and I think that when our negotiations wound up with the upset date of November 15 it was with the full realization on the part of both KPL and the producers that this is what was really meant, certainly by the producers. I think they really feel [44] that they do have other possible markets for the gas and if they cannot conclude this situation and know where they are, and so forth, that they might well elect to upset the contracts, as provided.

Q In the event your contracts as proposed in this proceeding are not approved by the Commission, what would

be the effect on KPL's investment in the Spivey-Grabs Field?

A Well, it would be useless, in a sense. After all, if we don't have any gas to take from the Spivey Field, then we would have the investment in gathering and compressor facilities as well as the transmission line from Spivey to Calista that would be of no value to us.

CROSS-EXAMINATION

BY MR. ALDERSON (for the Kansas Corporation Commission):

* * * * *

[67] Q Let's turn to Section 4, which Mr. Schell has mentioned. [68] The entire section concerns the effective date and the term of the contract. Paragraph 4.1 provides for the effective date prior to the expiration of the existing contract, and Paragraph 4.3, as Mr. Schell mentioned, provides for automatic termination of these contracts. Now, why did you provide in these contracts for an effective date prior to the termination of your existing contracts which, as we have discussed, have a much more favorable price for KPL?

[68] A Part of the negotiations with the producers —Keep in mind that at this point we are back to possibly April or May of this year. Part of the negotiations with the producers obviously related to price and their desire to get the best possible price as quickly as possible. At this point the Wichita contracts for $2.04 were in evidence.

* * * * *

[78] A There is a provision in the contract referred to as "Commission Approval". It's Section 8 on Page 12, in which we set out in there that we would have no obligation to pay for this increase, for escalation or for redetermination, until the effective date of the pass-on thereof as authorized by the KCC. Now, in the event that we make an application for the pass-on and it is

turned down, we have the options as set forth in 8.3. We have the option, to be exercised within 15 days after the KCC shall have rejected the pass-on, to pay the increase anyhow, even though we might not be able to pass it on.

Q What happens if you don't?

A If we don't elect to pass it on, then the seller shall have the option to terminate the contract on 30 days prior written notice.

Q Again, it seems that the Commission is becoming an integral part of your contract.

A Well, the Commission is, obviously, an integral part of our very corporate existence. We can't charge tariffs to any customers unless they are authorized by the Commission, and the gas purchasing business [79] these days has now gotten to the point where the magnitude of escalations, possible redeterminations, is such that we feel we must ask the Commission for this position.

Q Let me talk a minute about the justification for this escalation. You indicated that these were arm's length negotiations. Apparently, you felt that this was a fair increase.

A Yes, sir.

Q On what basis? You have already provided an increase, by your own testimony. Even though it says it's a dollar and a half based on the BTU adjustment, the figure you have used is a dollar fifty-three and three-quarters cents, an increase of [sic] 19 cents an Mcf. Now, on what basis do you think that an additional two cents is justified?

A Well, my answer can be quite short. You either provide an escalation or you don't buy gas these days. That is not exclusive with Spivey. This is the case with any gas negotiations you are into. There are actually two things you must do. You must provide escalation and you must provide price redetermination.

* * * * *

[84] Q Paragraph 6.7 provides for an upward adjustment in price. Can you explain the circumstances under which that occurs?

A Well, again, this is a paragraph that is becoming pretty much standard in all gas purchase contracts anymore. A lot of the interstate prices have been controlled by the F.P.C. We have no such situation in the State of Kansas. There is the possibility that this might occur in the State of Kansas. As a result of F.P.C. action, there is the possibility that the F.P.C. might come along one of these days and say that the area price in a given location, let's say in Spivey, should be $1.75. So all we have said here is that if that occurs we will meet that area price. Again, that is not exclusively in the Spivey contract any longer. We have [85] that in a number of contracts.

* * * * *

Q Under this procedure in 7.2 it requires the parties to mutually redetermine the price by considering three contracts under which the highest prices are actually being paid for flowing gas, and so forth, and then it sets forth some criteria that these contracts must [86] meet. What if the City of Wichita's contract meets all of these criteria?

A We would have to consider it as one of the contracts.

Q In other words, that $1.85, which is actually $2.04 with the BTU adjustment, you are bringing in another inflationary aspect of your price of $1.50 which within a couple of years won't even approach $1.50, will it, with all of these—

A I don't follow you when you say in a couple of years it won't approach a dollar and a half.

Q With all of these price adjustments and redeterminations and BTU adjustments, a dollar and a half is almost a mythical figure, isn't it?

A Well, I suppose that is a matter of opinion as to how mythical it may be. I'm sure we can expect it to go

up. There is no question in my mind but what the price of gas is going to go up wherever you are in the United States.

* * * * *

[87] Q But the amount required under those contracts for each of the first ten contract years was a scheduled amount, and for the 11th to 20th years the amount was 80 percent of the total daily productive capacity, not to exceed 40,000 Mcf per day. Under the proposed contract that we are looking at, KP&L is required to take or pay for 25 percent of the total open flow potential of all gas wells connected to KP&L's gathering system, with a maximum of 50,000 Mcf a day. Now, why was that maximum increased?

A It was increased perhaps more from wishful thinking or hopefulness on our part that there might be some development in Spivey that would increase open flows. In other words, there is a possibility—and I hope it's right—that some of the acreage that is open down there that perhaps is not dedicated to other parties, or that may be dedicated to KPL, could be found to be productive of gas. There is always the possibility that, with the higher prices that KPL will be paying, some of the producers may get in there and rework wells and increase open flows.

* * * * *

[96] Q Earlier, in response to a question by Mr. Grimes, you mentioned some other prospective purchases of gas, and I failed to note this. Could you reiterate those for me?

A W.I.E.C., Anadarko, and we had been told that there was a fertilizer plant that was interested in the Spivey [97] gas, and we had also understood that some industries were interested in it, and I think probably at least one other interstate pipeline company.

* * * * *

BY MR. SCHELL (for Clinton Oil Company [ERG's predecessor], Petroleum, Inc. and Pickrell Drilling Company, Intervenors):

[99] Q Mr. Williamson, the prior agreement, or the one that is [100] still in effect but going out, had a specific term, did it not?

A Yes, sir.

Q The proposed contract is for the life of the field; is that correct?

A That's correct.

Q If it's a life of the field contract, then that means that Kansas Power and Light will get every last molecule under that contract?

A I think that's correct, yes.

Q And the producers should require, as a result of that kind of dedication, the various provisions that Mr. Alderson has mentioned such as a redetermination of price, and so forth, as [sic] you go along because once the contract is signed then that is it, isn't it, and you live under it and the producers also stay under it and the gas remains with Kansas Power and Light?

A That's correct. I think that is a distinct advantage to both parties in this situation and certainly one that was considered in the negotiations.

* * * * *

REDIRECT EXAMINATION

BY MR. GRIMES:

[103] Q Mr. Williamson, Mr. Alderson asked about possible purchases by Peoples and Kansas Gas Supply in the Spivey-Grabs, and you and he I think related some prices related to those purchases. Do you have any knowledge as to the volumes involved in those contract purchases?

A Yes, I do.

[104] Q Are the volumes comparable to those in which you are dealing?

A Oh, much, much less.

Q Do you have any knowledge as to the term of the contract under which those two buyers might be buying in relation to a life of the field contract?

A I really do not, no, sir.

Q Would both the volume involved and the term of the contract affect the price?

A Very much so.

Amicus Brief

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No. 81-1370

IN THE

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OCTOBER TERM, 1982

ENERGY RESERVES GROUP, INC., *Appellant*,

v.

THE KANSAS POWER AND LIGHT COMPANY, *Appellee*.

On Appeal From The Supreme Court Of Kansas

JOINT MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* AND JOINT BRIEF *AMICUS CURIAE* OF ENERGY CONSUMERS AND PRODUCERS ASSOCIATION, OKLAHOMA INDEPENDENT PETROLEUM ASSOCIATION, SERVICE DRILLING COMPANY, HARRISON L. TOWNES, INC., SOUTHLAND DRILLING AND PRODUCTION COMPANY, L. O. WARD, AND AMERADA HESS CORPORATION IN SUPPORT OF APPELLANT.

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JOINT MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* OUT OF TIME IN SUPPORT OF APPELLANT

The Energy Consumers and Producers Association, Oklahoma Independent Petroleum Association, Service Drilling Company, Harrison L. Townes, Inc., Southland Drilling and Production Company, L. O. Ward, and Amerada Hess Corporation respectfully move this Court for leave to file the attached brief *amicus curiae* out of time in the above styled case pursuant to Supreme Court Rule 36.3.

The movants, hereinafter collectively referred to as the "Oklahoma Producers," are plaintiffs in litigation challenging the validity of the Oklahoma Natural Gas Price Protection Act, OKLA. STAT. tit. 52, §§ 260.1 - 260.13 (1981), a statute very similar to the Kansas Natural Gas Price Protection Act, KAN. STAT. ANN. §§ 55-

1401-55-1415 (Supp. 1981), which is the subject of the appeal now before this Court.[1] The defendants in the Oklahoma cases, the Oklahoma Corporation Commission and Oklahoma Natural Gas Company, *et al.* (the "Oklahoma Defendants"), have each filed briefs *amicus curiae* in this appeal. Their briefs discuss the facts of the Oklahoma cases and present arguments in support of the Oklahoma Act.

The briefs of the Oklahoma Defendants were filed in this Court on August 14, 1982 and came to the attention of movants a few days later. Until receipt of the briefs of the Oklahoma Defendants, the movants perceived no cause for seeking to be heard in this appeal and were fully aware of the time requirements of the Court's Rule 36. However, when the Oklahoma Defendants raised issues pertinent to the Oklahoma litigation and made incomplete statements concerning the facts of those cases and the Oklahoma Act, movants were obliged to come forward, though out of time. Matters raised by the Oklahoma Defendants impact directly upon issues in the Oklahoma cases and are set forth in the accompanying Brief in the Statements of Fact and Argument.

While the procedure, due to the circumstances caused by the Oklahoma Defendants, is unusual, it is not unique. Stern and Gressman indicate that a non-party may respond when similar issues are presented in another case in which he is involved. The means for seeking to be heard may be ". . . by seeking to file his own *amicus* brief in reply thereto." R. STERN & E. GRESSMAN, *SUPREME COURT PRACTICE* 727 (5th ed.).

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[1] *Energy Consumers and Producers Association* v. *Baker*, Civ. Nos. 79-320-D & 79-823-D (W.D. Okla. filed March 20 and 27, 1979). A decision has not yet been rendered in these cases, and due to this appeal they have been stayed.

Accordingly, the Oklahoma Producers move the Court for leave to file their brief *amicus curiae* and to do so out of time.

Respectfully submitted,

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STATEMENT OF INTEREST OF AMICI CURIAE

Energy Consumers and Producers Association, Oklahoma Independent Petroleum Association, Service Drilling Company, Harrison L. Townes, Inc., Southland Drilling and Production Company, L. O. Ward, and Amerada Hess Corporation (the "Oklahoma Producers"), are producers of natural gas within Oklahoma and associations comprised of oil and gas producers.

The Oklahoma Producers have an interest in this case because Oklahoma has enacted a statute substantially similar to the Kansas Act concerned herein. The Oklahoma Natural Gas Price Protection Act became effective March 19, 1979. OKLA STAT. tit. 52, §§ 260.1-260.13 (1981). The Kansas statute, which was enacted in May, 1979 is substantially similar to the Oklahoma Act.[1] See Appendix A to Brief of Oklahoma Natural Gas, *et al.*

The Oklahoma Producers have challenged the constitutional validity of the Oklahoma Act. These suits are pending in the United States District Court for the Western District of Oklahoma, and have been stayed pending outcome of this Appeal. *Energy Consumers and Producers Association, et al.*, v. *Baker, et al.*, Nos. 79-320-D & 79-823-D (U.S. D.C. W.D. Okla., filed March 20 and March 29, 1979). The Oklahoma Corporation Commission and Oklahoma Natural Gas Company, *et al.*, defendants and intervening defendants in the Oklahoma litigation, (the "Oklahoma Defendants") have recently filed briefs *amicus curiae* in this Appeal. This brief is filed because similar issues are presented in the pending Oklahoma cases which are impacted by the *Amicus* briefs of the Oklahoma Defendants. See, R. Stern & E. Gressman, *Supreme Court Practice* (5th ed.) 727.

The decision in this Appeal may affect the outcome of certain issues in the Oklahoma cases. In their *amicus* briefs the Oklahoma Defendants have made a number of statements and arguments concerning issues in the Okla-

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[1] The Kansas and Oklahoma statutes are referred to jointly as the "State Acts" and individually as the "Kansas Act" and "Oklahoma Act," respectively.

homa cases which we believe mandate the filing of this brief *amicus curiae*.

STATEMENT OF FACTS

We are confronted in the *amicus* brief of the Oklahoma Corporation Commission with a supposed legislative history of the passage of the Oklahoma Act.[2] While the recollections contained therein may be viewed generally as irrelevant to this appeal,[3] they do directly impact the litigation pending with respect to the Oklahoma Act and give a false impression of the existence of a legislative history within Oklahoma.

One of the principal issues in the Oklahoma litigation is the absolute failure of the legislature to identify what, if any, emergency the Act was intended to address within either the Act itself or any committee note or report. The Oklahoma legislature maintains no legislative history in the form of minutes or reports of committee sessions or otherwise and any intent or purpose of legislation must be found within the act itself. See e.g. *Haynes* v. *Caporal*, 571 P.2d 430, 434 (Okla. 1977); *Davis* v. *Childers*, 74 P.2d 930, 933 (Okla. 1938).

The purported "legislative history" contained in the Brief of the Oklahoma Corporation Commission and numerous other statements within the Briefs of the Oklahoma Defendants give rise to a number of false or distorted impressions and behoove the Oklahoma Producers to file this Brief in response thereto.

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[2] Brief of *Amicus Curiae* Oklahoma Corporation Commission ("OCC Brief"), pages 8-11.

[3] This section of the OCC Brief is apparently based upon the memory of the author. OCC Brief, p. 9, footnote 25.

The brief *Amicus Curiae* of Oklahoma Natural Gas Company *et al.*[4] contains frequent references to stipulations filed in the Oklahoma litigation. Quite obviously, these stipulations do not form any part of the record in this appeal and we believe selective reference and quotation from them to be blatantly inappropriate and unfair.

The Oklahoma Defendants further attempt to cloud the absence of price legislation within Oklahoma prior to enactment of the Oklahoma Act. Oklahoma had never previously imposed a maximum price on the intrastate sale of natural gas. Intrastate prices were subject only to traditional free market forces.

SUMMARY OF ARGUMENT

I. The Oklahoma legislature totally failed to identify any emergency which mandated the adoption of the Oklahoma Act. Without identification of the precipitating emergency, legislation imposing the obligation of contract cannot be meaningfully reviewed and the Court will not engage in mere speculation.

II. The State Acts impair the obligation of contracts as opposed to their enforcement. Natural gas producers will never receive the money which they would otherwise have been paid.

III. Oklahoma has never previously regulated the maximum price of natural gas. The Briefs of the Oklahoma Defendants attempt to create the false impression of a climate of active state price regulation. Natural gas producers relied upon the traditional free market in determining to sell to intrastate purchasers.

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[4] Referred to herein as "ONG Brief."

IV. Section 602 of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3432 (Supp. IV 1980) ("NGPA") cannot authorize the states to impair contracts. Such consent is forbidden absolutely by the United States Constitution.

ARGUMENT

I. INTRODUCTION

The natural gas utilities in this Appeal contend that their contracts with producers may be rewritten to their benefit by the legislatures of Oklahoma and Kansas under the guise of some supposed consumerism. However, the State Acts contravene the Contract Clause by impairing the contracts of the producers severely.

In the first decision dealing with the Contract Clause, Chief Justice Marshall stated that: "[w]hatever respect might have been felt for the state sovereignties, it is not to be disguised, that the framers of the Constitution viewed, with some apprehension, the violent acts which might grow out of the feelings of the moment; and that the people of the United States, in adopting that instrument, have manifested a determination to shield themselves and their property from the effects of those sudden and strong passions to which men are exposed. The restrictions on the legislative power of the states are obviously founded in this sentiment; and the Constitution of the United States contains what may be deemed a bill of rights for the people of each state." *Fletcher* v. *Peck*, 10 U.S. (6 Cranch.) 87, 137 (1810). This statement is as impelling today as when written.

In the few cases in which this Court has permitted a temporary encroachment to the enforcement of contract, there has existed a public emergency. This occurred most notably in *Home Building & Loan Association* v. *Blaisdell*, 290 U.S. 398 (1934). In *Allied Structural Steel Co.* v.

Spannaus, 438 U.S. 234 (1978), the Court measured the legislation against each of the five tests prescribed in *Blaisdell;* holding that a serious deficiency with any one of the criteria would suffice to strike down the legislation. 438 U.S. at 242-43. The State Acts fall short of each test.

II.
THE OKLAHOMA LEGISLATURE TOTALLY FAILED TO IDENTIFY ANY EMERGENCY

This Court in *Blaisdell* emphasized that an emergency had been *declared* to exist by the state legislature and took notice of the emergency created by the Great Depression. The nature of the emergency was equated to ". . . a great public calamity such as fire, flood, or earthquake." 290 U.S. at 439. The extensive declaration and findings of the state legislature were quoted verbatim in the *Blaisdell* opinion. 290 U.S. at 421-422. It is in rare situations, such as the Great Depression, that a state may properly use its police power to temporarily abate enforcement of certain contracts. The State Acts, however, contain no comparable declaration of emergency, and thus fail at the threshold.

In their *amicus* brief, Oklahoma Natural *et al.* attempt to create the false impression that the Oklahoma Legislature properly found the existence of an emergency within the framework of *Blaisdell.*[3] This statement cries out for amplification.

The Constitution of Oklahoma, Article 5, § 58, provides that acts of the Legislature become effective 90 days after adjournment of the legislative session unless the Legisla-

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[3] ONG Brief, p. 20.

ture expresses an emergency in the act. If an emergency is so expressed, the act becomes effective immediately upon execution by the Governor.[6] Such expressions are routine "[a]nd an emergency clause in the statute is given little or no significance in the interpretation of statutes, since such clauses are inserted, usually as a matter of form, to make the Act effective at once." 3 J. Sutherland, *Statutes and Statutory Construction*, § 71.12, at 363 (4th Ed. 1974).

As a result, in Oklahoma, the legislative expression of an "emergency" has a somewhat quaint meaning. During the 1979 session of legislature, when the Oklahoma Act was passed, over 60% of all bills contained the expression of an emergency.[7] The only reference to any emergency in

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[6] A manual, compiled by the Oklahoma Legislative Council for use by the Legislature, states:

> Some bills have an operative date written in them, but when there is no date specified in the bill, it becomes operative 90 days after the adjournment of the current session. The bill may become effective immediately upon gubernatorial action if it contains an emergency clause which declares that an emergency exists and the provisions of the act shall go into effect immediately after passage in order to protect the public peace, health and safety. The emergency clause can only be passed by a two-thirds majority of each house. The constitutional purpose of the 90-day delay was apparently to allow time for a referendum on any piece of legislation passed, but *in recent times the majority of bills passed have had emergency clauses* and the referendum is rarely, if ever, used. (Emphasis added). Oklahoma Legislature Manual, prepared by Oklahoma Legislative Council, page 33, (Jan. 1978).

[7] The various acts containing emergency clauses in the same legislative sessions included Senate Bill 296 (to establish an Archives and Records Commission), House Bill 1228 (providing for the appointment of an Assistant Mental Health Director), Senate Bill 71 (recreating the Will Rogers Memorial Commission), House Bill 1284 (establishing a Board of Cosmetology) and Senate Bill 120 (containing various measures including appropriations for the Jay, Okla.

the Oklahoma Act is in this connection, and most certainly does not rise to the police power standard of *Blaisdell*.

More importantly, however, the State Acts wholly fail to identify what, if any, emergency may have required their adoption. The requirement of *Blaisdell* that the legislature identify the impelling emergency is no mere technicality. Unless the legislature identifies and sets forth the basis for its actions, the tests enunciated in *Blaisdell* and *Allied* cannot be applied meaningfully. This cannot be accomplished by mere assumption or speculation as to legislative purpose or intent. See *Allied*, 438 U.S. at 247-248, in which this Court declined to consider the Minnesota Supreme Court's "speculation," unsupported by any official statements by the Minnesota Legislature, as to the legislative intent in enacting the challenged statute.

In Oklahoma, there is not one word of identification of any emergency by legislative report, any form of legislative history, or within the Oklahoma Act itself. Mere speculation as to an emergency does not meet the requirements of this Court.

The Oklahoma Producers submit it is more essential for the economic well-being of the collective States to maintain the protections provided in the Constitution than to override them for any reasons other than the absolutely most compelling. Whether the public interest may rest in lower fuel prices or in the increased development of our oil and gas reserves may be debated for years to come.

Huckleberry Festival, the Okeene, Okla. Rattlesnake Hunt, the Stroud, Okla. Brick Throw, the Wetumka, Okla. Sucker Day, and the Beaver, Okla. World Championship Cow Chip Throwing Contest).

However, there is a more important interest in reaffirming that contractual obligation still maintains its integrity and that persons have the freedom to plan their lives and business relationships based thereon.

III.
THE STATE ACTS IMPAIR THE OBLIGATIONS OF CONTRACTS AS OPPOSED TO THE ENFORCEMENT OF CONTRACTS

In *Blaisdell*, this Court held that "[t]he obligations of a contract are impaired by a law which renders them invalid or releases or extinguishes them . . . ." 290 U.S. at 431. This Court permitted the temporary moratorium on foreclosure of mortgages challenged in *Blaisdell*, because the statute does not impair the integrity of the mortgage indebtedness. The obligation for payment remains, 290 U.S. at 425. Contracts of the Minnesota mortgagees were not impaired, because they would eventually receive all they bargained for and, in the interim, would be paid rent. The Oklahoma and Kansas producers, on the other hand, will *never* receive the money that would have otherwise been paid to them under contract.

The crucial distinction is that "[t]he obligations of a contract are impaired by a law which renders them invalid or releases or extinguishes them. . . ." *Blaisdell*, 290 U.S. at 431. And, the Court held permissible only ". . . limited and temporary interpositions with respect to the enforcement of contracts as made necessary by great public calamity such as fire, flood, or earthquake." *Blaisdell*, 290 U.S. at 439.

The impairment of the producers' contracts goes directly to the obligation rather than merely to its enforcement. It does nothing to say that the State Acts

expire in 1984 for the obligation to pay money which would have otherwise been paid is destroyed absolutely.[8]

IV.
OKLAHOMA HAS NEVER PREVIOUSLY REGULATED THE MAXIMUM PRICE OF NATURAL GAS

The Oklahoma Attorney General in his *amicus* brief for the Oklahoma Corporation Commission creates the false impression that prior state regulation gave natural gas producers ample warning of future price limitation by the state and leaves an utterly incorrect impression as to the history of regulation within Oklahoma.[9] While Oklahoma, like most producing states, has appropriately regulated oil and gas exploration for environmental and conservation purposes, the State has consistently maintained a free market with respect to the intrastate sale of oil or natural gas. Prior to passage of the Oklahoma Act, the State had never imposed a maximum price on the first sale of natural gas.

Intrastate prices in Oklahoma have by conscious choice, been subject only to traditional market forces, and producers selling to intrastate purchasers were typically able to receive a higher price than those established by the FPC for the interstate market. Through this free

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[8] Even if the Oklahoma Act is struck down, the Producers will only receive the payments denied in monthly installments over a period not yet determined. This is so because the Oklahoma Legislature, anticipating a final judgment declaring the Price Protection Act invalid, provided for such monthly payments. See OKLA. STAT. tit. 52, § 260.11 (1981). Notably this anticipatory bill likewise contains the routine "emergency" declaration.

[9] OCC Brief, pp. 25-26.

market mechanism, Oklahoma fostered the development of its natural resources.

One must view with suspicion the "memory" of the Oklahoma Attorney General as noted in his Statement of Facts,[10] for his memory has failed him with respect to Oklahoma's historic free market for the sale of natural gas. While many authorities are extant as to the absence of prior legislation, none are more succinct than the statement of the same Attorney General in a brief filed on August 14, 1979 (the year of enactment of the Oklahoma Act):

> The producing states have chosen, within their borders, to allow producers and consumers of gas to contract for gas supplies at mutually agreeable prices. This system is a result of a conscious choice based upon years of experience and good conservation practices. Such intrastate freemarket systems have fostered development of natural gas resources by providing a stable intrastate market. Industries, attracted by the availability of natural gas, have established facilities in producing states where they could be assured of constant supply of essential natural gas. Traditionally, prices received by producers have been higher in the intrastate system than interstate rates, as local consumers have been willing to pay a premium for assured delivery, somewhat offset by reduced costs of transportation.
>
> Memorandum Brief in support of Plaintiff's Motion for Summary Judgment in *State of Oklahoma, et al.* v. *Federal Energy Regulatory Commission, et al.*, No. CIV-78-1251-T (U.S.D.C.W.D. Okla.) pp.4-5

This Court recognized in *Allied* a citizen's right to rely upon the prior pronouncements of his government. In

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[10] OCC Brief, p. 9, footnote 25.

entering long term contracts for the intrastate sale of natural gas, the Oklahoma Producers were relying upon the "conscious choice" of the State to foster a free intrastate market. Now, by passage of the State Acts, Kansas and Oklahoma seek to impose severe retroactive limitations on contracts which were never before regulated.

V.
SECTION 602 OF THE NGPA CANNOT AUTHORIZE THE STATES TO IMPAIR CONTRACTS

The Oklahoma Corporation Commission argues that "Congress explicitly recognized the legitimacy of state action in controlling indefinite price escalator clauses by the passage of Section 602 of the NGPA." OCC Brief, p. 25. Irrespective of whether the unique provisions of § 602 represent some purported delegation to the states or some presumed ceding of Congressional authority, the Congress may *not* constitutionally authorize or consent to an impairment by the states of the obligation of contract. Any such delegation or consent if forbidden *absolutely* by Article I, § 10 of the Constitution. No power under the government may make such an act valid or dispense with the Constitutional prohibition. *Rhode Island* v. *Massachusetts*, 37 U.S. 657 (1938).

Article I, § 10, represents a knowing relinquishment by the states to the federal government of certain rights which the States had previously enjoyed. Its purpose was to erect a "constitutional bulwark in favour of personal security and private rights." *The Federalist* No. 44 (J. Madison). Article I, § 10, of the United States Constitution provides:

> No state shall enter into any Treaty, Alliance, or Confederation; grant Letters of Marque and Repris-

> al; coin Money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts; pass any Bill of Attainder; ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.
>
> No State shall, *without the Consent of the Congress*, lay any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing its inspection Laws; and the net Produce of all Duties and Imposts, laid by any State on Imports or Exports, shall be for the Use of the Treasury of the United States; and all such Laws shall be subject to its revision and Control of the Congress.
>
> No State shall, *without the Consent of the Congress*, lay any Duty of Tonnage, keep Troops, or Ships of War in time of Peace, enter into any Agreement or Compact with another State, or with a foreign Power, or engage in War, unless actually invaded, or in such imminent Danger as will not admit of delay. (Italics supplied)

The phrase "without the Consent of Congress" is strikingly absent from the first clause of Article I, § 10; although expressly included in the second and third clauses. Congress may delegate to the states the power to keep troops or to enter into an agreement with another state, but Congress is prohibited absolutely from delegating or ceding to the states the power to coin money, grant any title of nobility or *impair the obligation of contracts*.

In *Holmes* v. *Jennison*, 39 U.S. 540 (1840) the Court interprets Article I, § 10 at pages 570 and 571 as follows:

> In the first paragraph, *the limitations are absolute* and unconditional; in the second, the forbidden powers may be exercised with the consent of Congress.
>
> * * *
>
> When therefore, the second clause declares that no state shall enter into "any agreement or compact"

> with a foreign power without the assent of Congress, the words "agreement" and "compact" cannot be construed as synonymous with one another; but still less can either of them be held to mean the same thing with the word "treaty" *in the preceding clause, into which the states are positively and unconditionally forbidden to enter; and which even the consent of Congress could not authorize.* (Italics supplied)

Whatever § 602 of the NGPA may represent, it cannot authorize a state to impair the obligation of contract. The prohibition of the Constitution is unqualified and absolute.

CONCLUSION

The Briefs of the utilities would lead one to conclude that a determination of the unconstitutionality of the State Acts would strip state legislatures of the power to address serious public issues. This is utter nonsense. The states have many meaningful tools through which to address public needs other than through impairment of contract. Moreover, where required by true public emergency, the Court has recognized that even this remedy may be available.

The Kansas and Oklahoma legislatures, however, have flouted the criteria and circumstances painstakingly established by this Court to justify a legislative impairment of contract. The State Acts are void of even the slightest attempt to identify what emergency may have required their passage or to tailor the remedies adopted to established Constitutional limitations. If the States are to enact such extreme remedies, they must scrupulously adhere to Constitutional prerequisites. Anything less is a mockery of the Contract Clause.

For the foregoing reasons, this Court should reverse the decision of the Kansas Supreme Court.

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No. 81-1370

In the Supreme Court of the United States

October Term, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

vs.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF KANSAS

BRIEF OF KANSAS LEGAL SERVICES AMICUS CURIAE

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No. 81-1370

In the Supreme Court of the United States

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ENERGY RESERVES GROUP, INC.,
Appellant,

vs.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF KANSAS

BRIEF OF KANSAS LEGAL SERVICES AMICUS CURIAE

INTEREST OF AMICUS CURIAE

Amicus Kansas Legal Services, Inc. (KLS) submits this brief in support of Appellee, and adopts Appellee's Statement of the Case and Questions Presented.

Kansas Legal Services is a non-profit, tax-exempt corporation organized under the laws of Kansas for the purpose of providing free legal assistance to low-income Kansans in non-fee-producing civil cases pursuant to the provisions of the Legal Services Corporation Act.[1] To meet the legal needs of low-income Kansans, KLS main-

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1. 42 U.S.C. Sections 2996 *et seq.*

tains 10 field offices across the state which are augmented with the support of a network of retained private attorneys. The KLS system makes legal services available to the over 275,000 low-income Kansans[2] residing in all 105 Kansas counties. In a typical year, KLS will complete 12,000-15,000 cases.

The rapid, unrelenting increases in energy costs in Kansas since the mid-1970's have significantly multiplied the number of KLS clients seeking legal representation to protect their access to essential public utility service. As a result, KLS has experienced a deepening involvement in increasingly complex administrative, judicial, and appellate public utility litigation. By virtue of its role as the legal representative of the poor in the many facets of the Kansas energy debate, KLS has become aware of the importance of this appeal to Kansas in general and to certain low-income Kansans in particular.

Amicus KLS's interest in this case arises from the fact that Appellant challenges the constitutionality of the Kansas Natural Gas Price Protection Act (K.P.P.A.).[3] After careful consideration, KLS has concluded that the K.P.P.A. is a sound state law, fashioned of necessity in response to the unique economic dislocations associated with the implementation of the Natural Gas Policy Act of 1978 (N.G.P.A.)[4] in a gas-producing state where heavy consumer dependency on locally produced gas is the rule. From the point of view of Kansas Legal Services, the K.P.P.A. protects a substantial number of Kansas gas con-

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2. U.S. Bureau of the Census, *Census of Population*: 1970 Vol. I, "Characteristics of the Population," Part 18, Kansas, U.S. Government Printing Office, Washington, D.C., 1973, p. 226. *Note*: Release of 1980 census data is pending.

3. K.S.A. 55-1401 *et seq.* (1981 Supp.)

4. 15 U.S.C. Sections 3301 *et seq.*

sumers from anomalous and unjustifiable fly-up gas prices which result when pre-N.G.P.A. price escalation mechanisms are exaggerated out of context and allowed to escape through a narrow discontinuity in the otherwise comprehensive N.G.P.A. price control scheme. But for the intervention of the K.P.P.A., a minority of Kansas gas producers would reap windfall profits from an anachronistic juxtaposition of old contract terms with new federal law. Losing the public-spirited K.P.P.A. would enrich these few gas producers at the expense of Kansas gas consumers, corporate and private, while sending another costly ripple through the Kansas economy.

What leads KLS to seek active participation in this appeal is the compelling concern that the interests of Appellant Energy Reserves Group, Inc. (E.R.G.) and Appellee Kansas Power and Light Company (K.P.L.) are the corporate interests of a producer-seller of natural gas and its large public utility buyer. These are the interests regulated by the K.P.P.A.; they *do not* represent the interests which the K.P.P.A. was adopted to promote. The K.P.P.A., as described by the legislators who sponsored it,

> . . . represents an effort by the state of Kansas to minimize the impact on consumers of natural gas price increases of some intrastate gas from the present time (1979) through 1984. For a period of nearly six years, this bill would provide a modicum of restraint on some utility price increases.[5]

Yet, by the nature of this litigation, it becomes the lot of K.P.L., a utility which automatically passes its increased

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5. Special Comm. on Energy and Natural Resources, Report on 1979 HB 2680. This reproduced in the appendix to the jurisdictional statement. (J.S. App.). All cites are to the appendix hereinafter.

wholesale gas costs directly through to its consumers,[6] to defend a state law which attenuates certain wholesale gas rate increases. If K.P.L. fails, it will be the consumers, not K.P.L., who will shoulder the economic burden of defeat. In reality, Kansas and its gas consumers throughout the state who benefit from the protection of the K.P.P.A. are the true parties in interest here—not K.P.L.

It is the preservation of the consumer perspective in the lawsuit which brings KLS before this Court. In this brief, *Amicus* KLS will concern itself with the consumer interest which the Kansas Legislature sought to protect when it passed the K.P.P.A.

SUMMARY OF ARGUMENT

In this case Appellant, a natural gas producer, challenges the constitutionality of the K.P.P.A., a state law designed to control the rate of price increases for first sales of natural gas produced and sold in Kansas. Appellant's position is that the Kansas law infringes on Appellant's rights under pre-existing gas sale contracts. Resolution of the case requires balancing the police power doctrine against the Contract Clause guarantee. In striking the balance, the Court is given the opportunity to declare that E.R.G.'s contracts cannot simultaneously reach out to take advantage of self-serving legislation and evaporate in the face of legislation which promotes the public interest.

In this brief, *Amicus* will first show that Appellant E.R.G. takes this Court's decisions, *Allied Structural Steel v. Spannaus*, 438 U.S. 234 (1978) and *United States Trust*

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6. Per Kansas Corporation Commission Order, Docket No. 106,850-U (April 19, 1977) and subsequent Orders in this docket.

Co. v. New Jersey, 431 U.S. 1 (1977), out of context to create an improper Contract Clause test for the constitutionality of the K.P.P.A. and by so doing makes state economic regulation vulnerable to almost any Contract Clause attack. *Amicus* will next demonstrate that, in spite of Appellant's protests to the contrary, the K.P.P.A. does serve an important public purpose by providing both direct and indirect protection for Kansas energy consumers precisely in the manner contemplated by the Kansas Legislature and in harmony with the objectives of the federal price control legislation outlined in the N.G.P.A.

It will then be established that the K.P.P.A. was a reasonable means for the Kansas Legislature to adopt in response to N.G.P.A. In this context, it will be demonstrated that the contours of the K.P.P.A. were designed to complement the policy objectives of the N.G.P.A. while protecting Kansas consumers from abrupt and substantial gas price increases. It will further be shown that the K.P.P.A. was enacted in a logical, timely manner.

Finally, *Amicus* will show that there is no reason to believe that Appellant's contracts were infringed, arguing, in that alternative, that if infringement does exist, it is so slight that it cannot be said to amount to the substantial impairment necessary to invalidate the K.P.P.A. These arguments will be established by showing that the N.G.P.A. at no time extended to the Appellant the right to higher N.G.P.A. prices for its gas and that what Appellant argues is impairment of its contracts is nothing other than sound legislation preventing Appellant from reaping windfall profits at the expense of Kansas consumers.

ARGUMENT

I. In the instant case, the proper test for determining whether or not a state law impairs a contract is (1) whether the contractual impairment created by the statute is substantial when contrasted with the public purpose served by the statute, and (2) whether the statute itself reasonably furthers the public purpose.

Although the Contract Clause appears absolute and unequivocal on its face,[7] this Court has not applied it literally because such application would render the Clause "destructive of public interest by depriving the state of its prerogative of self protection." *W. B. Worthen Co. v. Thomas*, 292 U.S. 426, 433 (1934). In the face of the Contract Clause, a state "continues to possess authority to safeguard the vital interests of its people." *Home Building and Loan Association v. Blaisdell*, 290 U.S. 398, 434 (1934). Thus, this Court has long recognized that individuals may not nullify state regulatory prerogatives by making contracts regarding the things regulated. *Union Dry Goods Co. v. Georgia Public Service Corporation*, 248 U.S. 372 (1919); *Manigault v. Springs*, 199 U.S. 473 (1905); *Hudson Water Co. v. McCarter*, 209 U.S. 349 (1908); *Atlantic Coast Line R.R. v. Goldsboro*, 292 U.S. 548 (1914).

While recognizing the need for states to protect their vital interests in the face of the Contract Clause, this Court has recently invalidated certain state laws on Contract Clause grounds where the contractual impairment involved was particularly strong and the state interest was extremely limited in scope or self-serving.

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7. The Contract Clause provides that "(n)o state shall . . . pass any . . . law impairing the obligation of contracts. . ."

These two cases, *Allied*, supra, and *United States Trust*, supra, are the linchpins of Appellant E.R.G.'s case. From these cases, Appellant derives what is asserted to be the singular test for the constitutionality of a state law undergoing a Contract Clause analysis. According to E.R.G., a statute fails to pass muster when "it (a) works a substantial impairment of contractual obligations, (b) does not address an important social problem, and (c) is not (i) a necessary and (ii) reasonable means to achieve the statute's ostensible purpose". Br. E.R.G. at 15. While this test may be derived from *Allied* and *United States Trust*, it does not inevitably follow that this is the exclusive yardstick to be applied when measuring the K.P.P.A. against the Contract Clause. The fallacy in Appellant's assertion lies in the fact that what Appellant discerns to be the proper test has been plucked in the abstract from the reasoning of *Allied* and *United States Trust* with insufficient regard for the facts which led to the Court's reasoning.

What is overlooked by Appellant's approach is that all Contract Clause cases decided in this century recognize the need for states to retain their police powers. It is only when a state uses its legislative prerogatives to overreach in its own contractual relationships (*United States Trust*), or where a state law, narrow in scope, unreasonably and severely impairs an obligation of an existing contract (*Allied*) that Contract Clause may be used to invalidate a state statute.

Appellant urges that the holding of this Court, in *United States Trust*, creates a "necessity test" as part of a proper Contract Clause analysis for all contracts regardless of whether the state is a contracting party. The necessity test, as applied in *United States Trust*, determines whether means exist, other than a state statute

impairing a contract, by which the state can accomplish the stated public purpose. If other means are found to be available, the statute violates the Contract Clause. At the practical level, this test, if applied to all contractual relationships, would require that a state legislature eliminate all other policy choices to achieve a given public purpose before impairing a contractual obligation.

In the context of *United States Trust*, where the state repealed its own statutory covenant, the necessity test was a viable means to limit the state's power to arbitrarily escape its own contractual obligations using the subterfuge that the abrogation of such obligation was in the public interest. Where the state is not a contracting party, however, the application of the necessity test would accomplish a far less desirable result.

If this Court were to broaden the Contract Clause analysis, making a necessity test applicable to all contracts, the police power of the states would be severely limited as a result. Private contracting parties engaged in economic ventures affecting the public health, welfare, and safety, could evade any future government regulation by simply making contracts covering such a contingency. In such a situation, with the burden on the state legislature to show that a statute impairing such a contract was the only means available to accomplish the stated public purpose, and with the limitless number of solutions that a creative mind can develop in response to a given problem, state legislatures might well be paralyzed in dealing with pressing public needs. This Court has long recognized that this result is unacceptable and has applied the Contract Clause accordingly in the past.

In sum, while it is recognized that the power of the state to "modify or affect the obligation of contracts is not without limit", it has also been made clear by the de-

cisions of this Court that the constitutional limitation cannot be construed to destroy the reserved state power of self protection. *City of El Paso v. Simmons*, 379 U.S. 497 (1965) at 509. *Amicus* KLS asserts, therefore, that the proper test to be employed to determine if a particular statute violates the Contract Clause is whether the legislation is based "upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption". *United States Trust*, supra, at 22. In applying Contract Clause analysis to a particular statute, this Court's analysis evaluates: (1) whether the contractual impairment created by the statute is substantial when contrasted with the public purpose served by the statute, and (2) whether the statute itself reasonably furthers such public purpose. The stricter test of *United States Trust* does not, as Appellant believes, apply in all cases where statutes are tested against the Contract Clause. The *United States Trust* test is reserved for the unusual cases in which the state itself has by legislation upset the contractual commitments which it voluntarily accepted. In the absence of a contract to which the state is a party, the traditional test is sufficient and the *United States Trust* test is not activated.

II. The K.P.P.A. is a reasonable means to serve an important public purpose.

A. The K.P.P.A. serves an important public purpose.

In the view of KLS the enactment of the N.G.P.A. by Congress justified the adoption of the K.P.P.A. by the Kansas Legislature because (a) the Kansas Legislature has had a traditional interest in protecting natural gas consumers from exploitation in the marketplace; (b) the N.G.P.A. would have caused a rapid and substantial escalation in price for a significant amount of existing intrastate gas

but for the K.P.P.A.; (c) the effect of large price increases for existing intrastate natural gas would have had a serious impact on consumers; and (d) the K.P.P.A. is totally consistent with Congressional Policy, as expressed in the N.G.P.A., because it does not interfere with the stimulation of new gas production, but softens the impact of high gas prices on the consumer by limiting price increases for existing intrastate natural gas.

(a) The State of Kansas has been vigorous in protecting its citizens from exploitation in the natural gas marketplace. Legislative authority for the regulation of natural gas pipeline companies was first created in 1911.[8] Those provisions, now codified at K.S.A. 66-101 *et seq.*, authorize the Kansas Corporation Commission to regulate natural gas pipelines, K.S.A. 66-104, and to prescribe rates if the rates changed by the pipelines are found after a hearing to be "unjust, unreasonable, unfair, unjustly discriminatory or unduly preferential". K.S.A. 66-113.

Initially, under the 1911 Act, the predecessor to the Kansas Corporation Commission, the Public Utilities Commission sought to regulate prices charged by interstate natural gas pipelines as well as local retailers. The power of the Public Utilities Commission to regulate the interstate market was upheld by the Kansas Supreme Court on the basis that Congress had not acted to regulate interstate pipelines and that the state had the power to regulate in the absence of Congressional action, *State Ex Rel. Helm v. Kansas Natural Gas Company*, 111 Kan. 809 (1922) at 812; but this Court reversed, holding that Congress had the sole power to regulate interstate pipelines, and that in the absence of such regulation "that particular commerce (would) be free from regulation", *Missouri Ex Rel. Barrett v. Kansas Natural Gas Company*, 265 U.S. 298 (1924).

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8. Sess. Laws 1911, ch. 238.

During the period between 1924, when *Missouri Ex Rel. Barrett,* supra, was decided, and 1938, the sole regulation of the natural gas industry was intrastate rate regulation by state utility commissions. Under this system, the state utility commission in Kansas remained vigorous in fulfilling its consumer protection obligations, at times exceeding its statutory and constitutional authority.[9] In 1938 Congress recognized the national need to regulate the interstate price of natural gas because of rapid price increases in non-producing states.[10] In that year the Natural Gas Act (N.G.A.) became law.[11]

After the enactment of the N.G.A. in 1938, the regulation of the intrastate market was tied to interstate regulation by the Federal Power Commission (F.P.C.). Interstate as well as intrastate pipelines were subjected to price controls similar to those imposed on other public utilities. With natural gas buyers controlled in this way, the price which natural gas producers could demand for their product was necessarily depressed.

Eventually, however, large natural gas producers began to hike up the wellhead price of natural gas and interstate regulation of wellhead prices was determined to be desirable by this Court in *Phillips Petroleum v. Wisconsin,* 347 U.S. 672 (1954). In the *Phillips* case the issue was whether the F.P.C. had correctly interpreted the N.G.A. with respect to its limitation on the regulation of production[12] by concluding that the wellhead price of natural

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9. See *Wichita Gas Co. v. Public Service Commission of Kansas,* 2 F.Supp. 792 (1933), modified and reversed in part in *State Corporation Commission of Kansas v. Wichita Gas Co.,* 290 U.S. 561 (1934).

10. D. Davis, Energy Politics 91 (1974).

11. Pub.L. No. 75-688, 52 Stat. 821 (codified at 15 U.S.C. Sections 717 *et seq.*).

12. 15 U.S.C. Section 717(b).

gas could not be regulated by the agency. This interpretation led the Attorney General of Wisconsin to sue Phillips Petroleum Company because an increase in the price which Phillips charged to the Wisconsin pipeline had caused increased natural gas charges to Wisconsin consumers. Reasoning that the purpose of the N.G.A. was to protect consumers against "exploitation at the hands of natural gas companies", 347 U.S. at 685, this Court concluded that the F.P.C. was mandated by the N.G.A. to regulate both wellhead prices charged by independent natural gas producers and the prices charged by pipelines.

After *Phillips*, supra, was decided, as a result of subsequent interstate wellhead price regulation by the F.P.C., intrastate regulation of wellhead prices became largely unnecessary. This was because "intrastate markets (were) . . . protected from nationwide demand by regulation of interstate prices".[13] Clearly, with a limited intrastate demand for natural gas at a price higher than the interstate price, coupled with an excess of supply in producing states, economic factors alone acted as a damper on high intrastate prices.[14]

An analysis of prices paid by Kansas consumers for natural gas at the retail level from 1960-1977 indicates that the intrastate market did not exhibit exorbitant prices. Indeed, in 1975, when, out of the 566.6 Billion Cubic Feet (B.C.F.) of natural gas consumed in Kansas, 297.7 B.C.F. was produced within the state,[15] the price paid by residential customers was only 60.23% of the national average

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13. Kumins, Natural Gas Regulation: *Problems and Options in Public Utility Rate Making in an Energy Conscious Environment*, at 48 (W. Sichel ed. 1979).

14. Id. at 50.

15. Committee Report, supra. See note 5 at 73a.

for residential consumers, 49.63% for commercial consumers, and 61.36% for industrial consumers.[16]

In sum, Appellant's contention that the absence of intrastate regulation of wellhead natural gas prices prior to the K.P.P.A. indicates that Kansas did not seek to protect the consumer from high natural gas prices in the past, is without merit. Since 1911, Kansas has sought vigorously to protect consumers by regulating the distribution and retail sale of natural gas. With interstate regulation of natural gas pipelines in 1938, and subsequent regulation of wellhead prices in 1954, intrastate regulation of wellhead prices was largely unnecessary because of economic forces inherent in the interplay between the interstate regulated market and the intrastate market. Based on the foregoing, it is clear that interstate regulation by the F.P.C., when combined with intrastate regulation at the retail level by the Kansas Corporation Commission, was adequate to protect consumers from gas prices which were out of proportion to those paid nationwide. It was only with the enactment of the N.G.P.A. that Kansas was faced with the need to control wellhead price increases for existing intrastate gas.

(b) It is clear that the Kansas Legislature had a reasonable basis to believe that the N.G.P.A. may have caused a rapid price increase for a significant amount of natural gas under existing intrastate purchase contracts having price escalation clauses. When it considered the K.P.P.A., the Legislature determined that in 1978, of the 866.6 B.C.F. which was produced in Kansas, 135.0 B.C.F. went to intrastate market and 731.6 B.C.F. went to the interstate market.[17] Although no figures are available to KLS for

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16. Kansas Energy Office, Kansas Energy Profiles at V-66 (1979).

17. Committee Report, J.S. App. at 73a, see note 16, supra.

total Kansas natural gas consumption in 1978, in 1977 consumption was about 508.742 B.C.F., and it was 515.197 B.C.F. in 1976.[18] Thus, if gas usage in these two prior years is an indication it can be concluded that a significant percentage of the gas consumed in Kansas in 1978 was produced intrastate. Of the total amount of intrastate gas used in Kansas, the Legislature determined that in 1978, 50 B.C.F. was subject to indefinite price escalation clauses such as those at issue here. Thus, approximately 10% of the gas consumed in Kansas in 1978 would have been subject to price escalation but for the K.P.P.A.

The K.P.P.A. limits the effect of price escalation clauses such as those under consideration here. In particular, K.S.A. 55-1404 states that neither the "price allowed to be paid pursuant to federal legislation or any regulation by an agency implementing such legislation" nor "the price paid or to be paid for any sale of natural gas in the state of Kansas shall be taken into account in applying any indefinite price escalation clause" in a contract subject to the Act. The practical effect of this provision was to limit Appellant's rights to increased prices, either as a result of the governmental pricing clause of its contract,[19] or the price redetermination provisions of its contract[20]. In this connection, Appellant is but one of many producers restricted by the K.P.P.A.[21]

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18. Energy Profiles, supra. See note 17 at V-41.

19. The governmental pricing clause is found at J.S. App. 66a. It is Section 6.7 of the Gas Purchase Contract and Section 8.5 of the Residue Gas Contract.

20. The price redetermination provisions are found at J.S. App. 67a-69a. These are embodied in Section 7 of the Gas Purchase Contract and Section 9 of the Residue Gas Contract.

21. For examples of other contractual price escalation clauses regulated by the K.P.P.A. See: *Mesa Petroleum Co. v. The Kansas Power and Light Co.*, 229 Kan. 631, clarified, 230 Kan. 166 (1981), cert. denied, ... U.S. ....., 50 U.S.L.W. 3592 (1982); *Edmiston v. State Corporation Commission*, slip op. (D. Kan. Nov. 24, 1980), as modified, Id. (D. Kan. Jan. 13, 1981), appeal docketed, No. 81-1197 (10th Cir. Feb. 23, 1981).

Section 105 of the N.G.P.A.[22] provided for the national regulation of intrastate natural gas wellhead prices for the first time. Under its provisions, the price to be paid for existing natural gas under intrastate contracts was limited to the Section 102 price,[23] or the price under the terms of the existing contract. Appellant contends that Section 105 was designed to allow price escalation clauses such as those at issue to operate to the Section 102 price level on Dec. 1, 1978. Thus, under Appellant's theory, when the N.G.P.A. was enacted, the government pricing clause of the contract was activated, and the Section 102 price was due under the terms of the contract. Whether this is true or not, the Kansas Legislature had a reasonable basis to believe that the K.P.P.A. was necessary as a means to preclude such price escalations.[24] The legislative committee considering the K.P.P.A. concluded that "the price of intrastate gas affected by H.B. 2680 (now the K.P.P.A.) would be $1.672 per M.M.B.T.U. as compared with $2.156

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22. 15 U.S.C. § 3315.

23. Section 102 of the N.G.P.A. is codified at 15 U.S.C. § 3312. In the Appendix to E.R.G.'s Brief on the merits it is indicated that the price paid due to the operation of the K.P.P.A. is significantly less than the Section 102 price. For instance in July 1982, the Section 102 price is $3.152 while the current contract price is $2.096.

24. Section 105 of the N.G.P.A., codified at 15 U.S.C. § 3315, is not a hallmark of clarity with respect to its effect on indefinite price escalation clauses in existing intrastate gas contracts. The Federal Energy Regulating Commission (F.E.R.C.) first determined that the N.G.P.A. did not trigger indefinite price escalation clauses in intrastate contracts on December 1, 1978. 43 F.Reg. 56448, 56550-51 (Dec. 1, 1978). Later the F.E.R.C. changed its position and allowed price escalation provisions in existing intrastate contracts to operate according to their terms subject to N.G.P.A. price ceilings. 44 F.Reg. 16895; 16904 (March 20, 1979), codified at 18 C.F.R. § 270.205(b)(1) and (b)(2). With these varying interpretations, the Kansas Legislature could have well believed that the N.G.P.A. would have caused a rapid increase in prices on December 1, 1978, due to governmental pricing clauses, or that a rapid increase in price would occur in the future due to the operation of price redetermination provisions in existing intrastate contracts.

M.M.B.T.U. without the bill, a 29 percent savings", and further concluded that "over time the gap between the two prices would increase".[25] The price gap was substantial in 1979 and as predicted is more substantial now.[26] This provides "ample reason" for the enactment of the K.P.P.A.

(c) Appellant complains that the K.P.P.A. is special legislation affecting only a small number of persons. While it may be true that only a small number of organizations are affected by the K.P.P.A., it is clear that since these organizations are public utilities—such as Appellee—the impact of the K.P.P.A. is broadly felt.

Seventy-five percent of all Kansas households are heated with natural gas. Of this number, approximately 107,000[27] are customers of K.P.L. within the "main system", known as Rate Area A. Within the K.P.L. main system, intrastate gas is generally the exclusive source of supply. From a statewide perspective, these K.P.L. customers comprise about 13.2% of all 809,986 gas customers in Kansas.[28] Rate Area A encompasses all or part of 37

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25. Committee Report, J.S. App. at 76a-77a.

26. See note 23, supra.

27. See Security and Exchange Commission, Form 10-K, Part I, p. 7, filed by Kansas Power and Light Company for fiscal year ended December 31, 1981.

28. Here KLS has assumed the total number of Kansas gas customers to be 809,986. This figure is produced as follows: The K.C.C. reports that the 25 investor-owned gas companies it regulates have 753,406 total customers based on cumulative totals from F.E.R.C. Form 1, Annual Report submissions for 1981. In the document, *Municipal Utilities Annual Report*, League of Kansas Municipalities, Aug., 1981, p. 8, the League of Municipalities shows 28,014 total customers for the 69 municipally-owned (unregulated) gas utilities. In addition, there are 13 privately-owned but unregulated gas companies operating in Kansas. The 7 largest of these companies reported to KLS a total of 27,566 current customers. KLS estimates that the 6 not reporting have no more than a combined total of 1,000 customers based on the population of the areas they serve, the largest of which has a

(Continued on following page)

Kansas counties and includes the cities of Great Bend, population 16,133; Manhattan, population 27,575; McPherson, population 10,851; and Salina, population 37,714.[29] Of the total population of 217,945 persons for the counties within Rate Area A, 12.3% are at or below the poverty level.[30]

While no data are available on the impact of high energy costs on low income Kansans, studies have been done which indicate such impacts on a national basis. In March of 1975, the Federal Energy Administration released a study which indicated that "(t)he elderly poor consume less energy than any other age-income group, including the younger poor, and yet they spend a much higher proportion of their total budget on energy expenditure."[31]

In December of 1976, the Federal Energy Administration released another study which dealt specifically with the impact of energy price increases on low income consumers. This study indicated that "although low income households spent less on energy and experienced small absolute increases in expenditures, these expenditures and increases represented a much larger proportion

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Footnote continued—

population of only 870 persons. The only truly significant privately-owned, unregulated gas companies are Kansas Public Service, which serves Lawrence, Kansas (pop. 45,698), and has 18,237 customers and the Liberal Gas Company which serves Liberal, Kansas (pop. 13,471) and has 6,422 customers.

29. Counties and cities in K.P.L. Rate Area A are listed in K.P.L.'s current rate filings on file with the K.C.C. appearing in K.C.C. Form RF, Schedule, Index-81, Sheets 1 and 2, July 28, 1980.

30. Population and demographic figures are from the 1970 Census. See note 2, supra.

31. Federal Energy Administration, Pub. No. 6-53, The Effects of Rising Energy Prices on the Low and Moderate Income Elderly, at 1.7 (Mar., 1975).

of their disposable income than for higher income households—roughly ten times larger."[32]

It is clear that energy prices have not decreased since the time these studies were completed. Due to the N.G.P.A., they have risen substantially. In this context it seems clear that for those making low wages or on fixed incomes, an increase in the percentage of income spent on energy can have dramatic effects. People are forced to forego food and other basic necessities of life in order to pay their gas bill. There is no reason to believe that Kansas low income energy consumers are different from those represented in these nationwide studies.

Due to the dramatic impact of high energy prices on low income consumers, federal legislation has been developed which gives limited funds to states to provide some relief for low income consumers.[33]

Consideration of Kansas' distribution of energy assistance to needy consumers under this program during the past winter (December-March, 1981-1982) reveals the scope of the gas price problem. The sum of $8,309,072 was used to assist 62,008 needy Kansans in paying their bills, another $1,135,159 was distributed to 7,526 needy persons who had already received shut-off notices. Many of the latter received shut-off notices even after applying the first round of program benefits to their bills. Of the total $9,444,231 expended, 86.1% went to pay gas bills.[34] It is clear that

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32. Federal Energy Administration, Pub. No. PB-262 098, Impact of Energy Price Increases on Low-Income Families, at 6 (Dec., 1976).

33. Low-Income Home Energy Assistance Act of 1981, 42 U.S.C. §§ 8621 *et seq.*

34. Statistics provided to KLS by the Kansas Department of Social and Rehabilitation Services, Topeka, Kansas. This state agency is responsible for the distribution of Low-Income Home Energy Assistance Act funds in Kansas.

with budget cuts in welfare and other programs, any increase in consumer energy prices would create a situation where less money would have to go further in meeting a vital social need.

When considering the K.P.P.A., the legislative committee studying the bill estimated that, in the absence of the measure, $127.5 million would be transferred from consumers to gas producers.[35] The cost to the consumer of this massive transfer of wealth would have been reflected not only by higher prices in retail gas sales to residential consumers, but also in higher electric bills because of increased fuel costs to utilities using intrastate gas for electricity generation.

Finally, Appellant contends that the K.P.P.A. was an inappropriate consumer protection measure because increased prices for gas arising from price escalation clauses might not be passed on to consumers. Br. E.R.G. at 31. Appellant's argument is totally without merit. In the first place, it is axiomatic that a public utility is allowed to recover its cost of serving its customers by setting rates which compensate the utility for legitimate price increases incurred in continuing utility operations. More to the point, the Kansas Corporation Commission in 1977, issued an order which permitted Kansas regulated public utilities to recover their increased purchased gas costs automatically, without the necessity of seeking formal K.C.C. permission on a case-by-case.[36] To accept Appellant's argument is to adopt the point of view that natural gas utilities can be required to engage in deficit spending and to operate at a loss. Such a theory defies both existing law and reason.

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35. Committee Report, J.S. App. at 73(a).

36. K.C.C. Order. See note 6, supra.

(d) The N.G.P.A. was enacted to remedy shortages of gas in the interstate market. Regulated interstate prices under the N.G.A. for new gas were below unregulated intrastate prices. With low interstate prices stimulating demand in that market, and intrastate purchasers being able to easily outbid interstate purchasers, interstate shortages occurred.[37] This problem was "exacerbated" by the exceedingly cold winter of 1976-77.[38]

The N.G.P.A. contained a comprehensive scheme for regulating natural gas prices. Title I of the Act concerned wellhead pricing. An analysis of these provisions reveals they include (1) incentive pricing for new gas and price controls on intrastate gas to ensure adequate supplies in the interstate market,[39] and (2) maintenance of the N.G.A. price controls on old gas to prevent price increases which would not serve to further the goal of increased production.[40] Under the N.G.P.A. regulation of old intrastate gas was left to states.[41]

The K.P.P.A. is totally consistent with the purpose of the N.G.P.A. It does not frustrate the national goal of stim-

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37. U.S. Dept. of Energy, DOE/PE-0031, A Study of Alternatives to the Natural Gas Policy Act of 1978 at 2 (Nov., 1981).

38. Id.

39. The price incentive portions of the act are found at § 102 (15 U.S.C. § 3312), § 103 (15 U.S.C. § 3313), § 107 (15 U.S.C. § 3317) § 108 (15 U.S.C. § 3318), and § 110 (15 U.S.C. § 3320).

40. Consumer Protection sections designed to prevent rapid increases in the price of old intrastate natural gas are found at § 104 (15 U.S.C. § 3314), § 106(b) (15 U.S.C. § 3316(a)), and § 109 (15 U.S.C. § 3319).

41. Under § 602 of the N.G.P.A. (15 U.S.C. § 3432) states are given the authority to regulate prices of natural gas provided that the regulated prices do not exceed the maximums established in the N.G.P.A. This authority specifically includes the authority to limit the operation of any indefinite price escalation clause. H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. (1978) pp. 124, 125.

ulated production but does protect consumers using old intrastate gas from rapid price increases due to the operation of indefinite price escalation clauses. Moreover, it is precisely the kind of state regulatory action anticipated by Congress when the N.G.P.A. was enacted.

B. The K.P.P.A. is a reasonable means to achieve the Legislature's stated goal.

Appellant asserts that the K.P.P.A. is "far from a reasonable measure for accomplishing the Legislature's stated goal" because of its "limited scope and abundant exceptions." Br. E.R.G. at 38. However, it is obvious from reading the Kansas measure in concert with the N.G.P.A. that its contours were shaped by that federal law, and that its objectives are similar.

First, the primary means utilized to protect consumers in the N.G.P.A. is to prevent rapid price increases for old interstate gas. The K.P.P.A. merely prevents price escalator clauses from dramatically increasing the price of old intrastate gas. These two measures are parallel and the K.P.P.A. is a reasonable means to assure that intrastate consumers are protected.

Further, the limited duration of the statute is not arbitrarily determined. December 1, 1978, is the effective date of the N.G.P.A., and December 31, 1984, is the last day that price escalation clauses remain unregulated by the N.G.P.A. Section 105(b)(3), 15 U.S.C. 3315(b)(3), of the N.G.P.A. regulates intrastate gas subject to price escalation provisions effective January 1, 1985.

Among the "abundant exceptions" cited by Appellant are those for gas from stripper wells, new reservoirs and new wells. Under the provisions of the K.P.P.A., after March 1, 1979, the price of this gas may escalate in accord

with contract terms to the rate it would receive "if it had been committed or dedicated interstate commerce." J.S. App. 61a-62a. Likewise, Appellant complains that the K.P.P.A. is limited in scope because it applies only to contracts made before April 20, 1977. All of these limitations and exclusions are reasonable. First, gas from stripper wells, new reservoirs, and new wells receives incentive price treatment under the N.G.P.A. Also, April 20, 1977, the date President Carter announced his energy plan, is used as a bench mark date throughout the N.G.P.A. to define gas prospectively eligible for incentive pricing [e.g. see Section 102(c)(1)(C) of the N.G.P.A., 15 U.S.C. Section 3312 (c)(1)(C)]. Not only is it reasonable to accord gas from stripper wells, new reservoirs, and new wells, as well as gas under contract after April 20, 1977, equal treatment in both the intrastate and interstate markets, it is also necessary to do so because otherwise intrastate shortages might occur from the resulting price differential. In sum, the exclusions in the K.P.P.A. are rational when considered in concert with the relevant provisions of the N.G.P.A.

Implicit in Appellant's argument is that the K.P.P.A. is unreasonable because it was hastily contrived and had retroactive impact. In this instance the reasonableness of the Legislature's action is readily apparent. The Kansas Legislature only meets for a portion of the year. In 1979, it convened on January 8, a little over one month after the N.G.P.A. became effective. The Legislature could only have responded to the N.G.P.A. after that date. Further, from January until March of 1979, it appeared as if the F.E.R.C. would limit the operation of intrastate price escalation provisions.[42] The K.P.P.A. was introduced on April 25, 1979, Br. E.R.G. at 8, assigned to committee on

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42. See note 24, supra.

May 4, 1979, Br. E.R.G. at 9, and on May 14, 1979, the K.P.P.A. was enacted, Br. E.R.G. at 11. Given the reality that without prompt legislative action, N.G.P.A. Section 102 prices may have applied by virtue of pre-existing indefinite price escalation clauses in intrastate contracts, the Legislature's actions in April and May, 1979, were not hasty, but necessary to achieve the desired result. Also, the Legislature acted in a reasonably timely manner in developing policy in response to the complex provisions of the N.G.P.A.

Appellant finally contends that the voluntary renegotiation provisions of the K.P.P.A. were arbitrary and thus rendered the entire Act unreasonable. While it is true that the Act does provide for voluntary renegotiation of contracts containing price escalation clauses, such renegotiation may be necessary to protect the integrity of the K.P.P.A. itself. These provisions act as a safety valve in case of arguable breach by a gas purchaser. In that case, a gas purchaser's ability to renegotiate terms of the contract and to protect its gas supply is preserved. Further, gas purchasers under such contracts are generally public utilities subject to state regulation. It is clear that, in the instant case, the Kansas Corporation Commission would not allow K.P.L. to renegotiate current contracts causing higher consumer prices unless good reasons for such renegotiation existed.

III. The K.P.P.A. only minimally impairs Appellant's contractual rights, if such impairments exist at all.

In the view of KLS it is doubtful that the Appellant's contractual rights were impaired by the K.P.P.A. because the contract was made, by its own terms, subject to all future state and federal laws. Moreover, in any event, Section 105(b)(1) of the N.G.P.A. would not have triggered

the governmental pricing provisions of the instant contracts. Finally, even if a contractual impairment is determined to exist, it is insignificant when contrasted with the purpose served by the K.P.P.A.

(a) It is basic that in a contract clause case "this court is bound to determine for itself whether there is a contract and its true meaning and effect". *Coolidge v. Long*, 282 U.S. 582 (1931) at 597. The contracts now before this Court contain a provision which subjects both their price redetermination provisions and the governmental pricing clause to "all relevant present and future state and federal laws" and which further provides that "(n)either party shall be held in default for failure to perform . . . if such failure is due to compliance with such laws". J.S. App. 69a-70a.

It is undisputed by the parties that the Appellant did not attempt to activate the price redetermination provisions of the contract until July 24, 1979, and the Court below so found. J.S. App. 10a. This was well after the K.P.P.A. was enacted and by virtue of the governmental regulation provisions of both contracts, the K.P.P.A. limited Appellant's right to price redetermination at that time. Likewise, the governmental pricing clauses in the instant contracts were ineffective because the K.P.P.A. precluded their operation from December 1, 1978.

(b) Moreover, circumstances are not such that Section 105(b)(1) of the N.G.P.A. would trigger the governmental pricing clause in the instant contracts. Section 105(b)(1) merely set price ceilings for old intrastate gas; it did not fix prices in the context of the governmental pricing clauses here at issue. The Conference report accompanying the N.G.P.A. states as follows:

> The conferees do not intend that the mere establishment of the ceiling prices under this Act shall

> trigger indefinite price escalator clauses in existing intrastate contracts. Once natural gas is sold pursuant to the ceiling prices under this Act, such clauses would be activated as limited by this section.[43]

Here, the Conferees recognized that *sales* of natural gas would trigger appropriate price escalation clauses, but did not intend that the price ceilings established by the N.G.P.A. would automatically escalate prices to the N.G.P.A. Section 102 level. Perhaps, the Conference report would support the argument that the sale of gas within Kansas under N.G.P.A. price ceilings would justify the activation of the price redetermination mechanism contained in the instant contracts; but, as pointed out above, the K.P.P.A. prospectively limited the operation of these provisions in the instant case. Therefore, no price increase under, either the governmental pricing clause or the price redetermination provisions of the instant contracts, results from the enactment of Section 105 of the N.G.P.A.

(c) If it is determined that Appellant's rights under the governmental pricing clause were impaired, notwithstanding the arguments above, it is still necessary to conclude that the impairment is slight when contrasted with the strong public purpose underlying the K.P.P.A. Here it is worthy of note that Appellant does not suggest that the K.P.P.A. has rendered its contracts with K.P.L. unprofitable. What Appellant asserts instead, is that but for the intervention of the K.P.P.A., its contracts with K.P.L. would have become a great deal more profitable than they were when E.R.G. committed itself to the contracts. This argument is considerably less persuasive than those existing in the *Allied* supra, and *United States Trust,* supra,

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43. H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. (1978) at 83.

decisions on which Appellant bases its case. In addition, the K.P.P.A. leaves untouched the generous provisions in the contracts which allow E.R.G. to routinely adjust prices to offset inflation. See, Section 8.1 of the Residue Gas Contract, J.S. App. at 66a. Finally, the terms of the contract make it clear that the parties E.R.G. and K.P.L. were subject to future state and federal laws. At the time the contract was drafted, no party could with certainty assume that the singular impact of any future laws would be to accelerate price increases. To endorse Appellant's point of view is to say that there was no risk of future laws which would attempt to moderate price increases. To complain after the fact that one law which appeared to accelerate price increases was wrongfully complemented by another which had a moderating influence is illogical; and this argument does not justify the conclusion that there was substantial impairment of Appellant's contractual expectations even if, in a technical sense, the K.P.P.A. impaired Appellant's rights under the instant contracts.

CONCLUSION

For the foregoing reasons, this Court should affirm the decision of the Kansas Supreme Court.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

BRIEF OF AMICUS CURIAE STATE CORPORATION COMMISSION OF THE STATE OF KANSAS IN SUPPORT OF APPELLEE THE KANSAS POWER AND LIGHT COMPANY

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INTEREST OF AMICUS CURIAE

The salient facts of this case are concisely stated in the Statement of the Case contained in appellee's brief. For purposes of brevity, *amicus* State Corporation Commission of the State of Kansas (State Commission) adopts appellee's Statement of the Case and Questions Presented.

Title I of the Natural Gas Policy Act of 1978 (NGPA) (15 U.S.C. § 3301, *et seq.*) established an intricate set of controls for the wellhead price of natural gas, including natural gas produced and marketed intrastate under existing contracts. (15 U.S.C. § 3315) The NGPA also

authorized the gas producing states to institute such price control legislation for intrastate gas as they might deem necessary and appropriate because of the passage of the NGPA. (15 U.S.C. § 3432(a).) Pursuant to this Congressional directive, the Kansas Legislature enacted the Kansas Natural Gas Price Protection Act (Price Protection Act) (K.S.A. § 55-1401 *et seq.* (1980 Supp.)), which established a ceiling price for natural gas produced and consumed within Kansas.

Amicus State Commission is a state administrative agency vested with broad regulatory authority over electric and gas utilities doing business in Kansas. This authority includes responsibility for making gas well category determinations pursuant to the NGPA (15 U.S.C. § 3413), and the implementation and enforcement of the provisions of the Price Protection Act (K.S.A. § 55-1409 (1980 Supp.)). As a consequence, the Commission has a substantial interest in assuring that the constitutionality of the Price Protection Act continues to be sustained, and that the NGPA and the Price Protection Act are interpreted in a consistent fashion.

SUMMARY OF ARGUMENT

But for the Price Protection Act, passage of the NGPA would have permitted intrastate gas producers to collect the NGPA § 102 new gas price for old intrastate gas, being sold under existing contracts, through the operation of indefinite price escalation clauses. Such an abrupt and unintended escalation of the price of intrastate gas would have caused significant economic dislocation in gas-producing states such as Kansas. In order to prevent this harm from occurring, the Kansas Legislature exercised its police power to regulate the price to be paid for intrastate gas. It did so by moderating the operation of indefinite price escalation clauses contained in existing contracts. As the Kansas Supreme Court properly held, in taking this action the Kansas Legislature acted in a

reasonable and moderate fashion, and the action taken was well within the bounds of that permitted by the Contract Clause of Article I, Section 10, of the Constitution. After applying the tests established in *Home Building & Loan Association v. Blaisdell*, 240 U.S. 398 (1934), *United States Trust Co. v. New Jersey*, 431 U.S. 1 (1977), and *Allied Structural Steel v. Spannaus*, 438 U.S. 234 (1978), the court below concluded, as have all other courts which have addressed this question, that the Price Protection Act is reasonable and necessary to deal with an important social problem, and imposes only a modest burden on the contracts which it affects.

(a) The passage of the NGPA radically altered federal policy regarding the pricing of natural gas. Absent state regulatory action, this policy reversal would have caused a major increase in intrastate gas prices and a substantial financial windfall for intrastate gas producers whose contracts contained indefinite price escalation clauses. This windfall would not have helped to increase the available supplies of new gas, the basic purpose of the high § 102 ceiling price contained in the NGPA. Congress recognized the dire consequences of such an unintended escalation of intrastate gas prices to producing states, and expressly authorized state legislatures to restrict the operation of indefinite price escalation clauses in existing contracts. 15 U.S.C. § 3432(a). The Kansas Legislature acted to address this "important general social problem," *Allied Structural Steel*, 438 U.S. at 247, by passing the Price Protection Act.

(b) The Price Protection Act is a carefully drawn statute designed to regulate the price of all intrastate gas which is both "reasonable" and "necessary" to address the important "economic problems" which the passage of the NGPA caused for gas producing states. *United States Trust*, 431 U.S. at 25. It is drafted to reach only those existing contracts containing escalation clauses effected by the passage of the NGPA. The stat-

ute allows the existing contracts, with all of their terms, to remain in effect, while establishing the NGPA § 109 ceiling price as a limit on the price escalation available for old intrastate gas. The limit so established does not freeze this price, but allows producers to collect a higher price under their contracts as the NGPA § 109 price escalates upwards. In accordance with the *Blaisdell* decision, 290 U.S. at 440, 445, the duration of this ceiling price for old intrastate gas is limited, coming to a complete end on December 31, 1984. Since the record in this case conclusively demonstrates the reasonableness and necessity of the Price Protection Act, it should be accorded the "presumption favoring legislative judgments as to the necessity and reasonableness of a particular measure . . ." (citation omitted) *Allied Structural Steel*, 438 U.S. at 247.

(c) The Price Protection Act imposes the type of modest burden the Court had in mind when it indicated that a "minimal alteration of contractual obligations may end the inquiry at the first stage." *Allied Structural Steel*, 438 U.S. at 244-45. This statute does not abrogate existing private contracts, nor does it excise from them any particular clause. While leaving the basic price clause of these contracts intact, the Price Protection Act moderates the operation of contingent indefinite price escalation clauses in the totally new gas-pricing environment brought about by the passage of the NGPA. By establishing an NGPA ceiling price for this intrastate gas, the Price Protection Act allows intrastate gas producers to reap a substantial financial benefit under their existing contracts. The Price Protection Act does not require these intrastate gas producers to disgorge these windfall profits, but operates to limit the size of the windfall received. Statutes such as this, "which restrict a party to those gains reasonably to be expected from the contract are not subject to attack under the Contract Clause." *El Paso v. Simmons*, 397 U.S. 497, 515 (1965).

2. The question of whether a specific intrastate gas contract permits, in the absence of state-level regulation, the collection of the NGPA § 102 price is dependent upon the specific language of the price escalation clause contained in the contract. In this case, the Kansas Supreme Court determined that the language contained in the ERG's contract was insufficient to justify escalation to the NGPA § 102 new gas price. Even had the language of the contract been sufficient to allow such escalation, the establishment of the NGPA § 109 price as the ceiling price for such gas by the Price Protection Act prohibited collection of the new gas price by ERG. The Kansas Supreme Court clearly understood that NGPA § 105(b) does not prohibit the operation of indefinite price escalation clauses.

ARGUMENT

I. Article I, Section 10 of the United States Constitution Permits States to Enact Price Regulations Which Modify Existing Private Contracts.

The fundamental question posed by this appeal is whether the Price Protection Act comports with the Contract Clause of Article I, Section 10 of the United States Constitution. That Clause provides that "no state . . . shall . . . pass any . . . Law impairing the obligation of contracts . . .". While a literal reading of this language would prohibit any state legislation which impinged upon an existing contract, this Court has long recognized that the "prohibition is not an absolute one." *Blaisdell*, 290 U.S. at 428. State legislatures may modify existing contractual relationships by exercising their inherent police powers. While affirming the continued vitality of the Contract Clause, the Court has established a standard of review which strikes a reasonable balance between the states' unquestioned right to enact legislation to ensure the public welfare, and the desirability of

protecting existing private contractual relationships.[1] In striking this balance, the Court has recognized that "states must possess broad power to adopt general regulatory measures without being concerned that private contracts will be impaired, or even destroyed, as a result." *United States Trust Co.*, 431 U.S. at 22.

In utilizing this balancing approach, the Court has sought to ". . . prevent the perversion of the [Contract] clause through its use as an instrument to throttle the capacity of states to protect their fundamental interests." *Blaisdell*, 290 U.S. at 444 (1934). It has done so by refraining from substituting its judgment for that of the legislatures as to what is the wisest course of action to follow, and by recognizing that "courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure." *United States Trust Co.*, 431 U.S. at 22 (1977).

The instant proceeding is a contract termination case which has raised the issue of the constitutionality of natural gas price control legislation passed by the Kansas Legislature. ERG sought judicial approval of its attempt to terminate its intrastate gas supply contract with The Kansas Power and Light Company (KP&L). Initially, ERG argued that the mere passage of the NGPA triggered the indefinite price escalation clause contained in the contract, thereby vesting ERG with the constitutional right to collect the NGPA § 102 new gas price for the old intrastate gas sold under an existing contract. At a later date ERG argued that the periodic price redetermination clause contained in the contract obligated KP&L to escalate the contract price up to the NGPA § 102 new

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[1] This balancing approach has been established by a consistent line of decisions. *See, Home Building & Loan Assn. v. Blaisdell*, 290 U.S. 398 (1934); *Veix v. Sixth Ward Building & Loan Assn.*, 310 U.S. 32 (1940); *El Paso v. Simmons*, 379 U.S. 497 (1965); *United States Trust Co. v. New Jersey*, 431 U.S. 1 (1977); and *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234 (1978).

gas price level upon redetermination. According to ERG, when KP&L declined to pay these escalated prices, ERG had the right to terminate the contract. Appellant's Brief at 5.

In its decision disposing of these two issues, the Kansas Supreme Court held that the contractual language contained in the indefinite price escalation clause was insufficient to warrant the collection of the NGPA § 102 price, which Congress intended to be paid for newly discovered gas. This determination was in conformity with the Congressional intent in passing the NGPA,[2] the FERC regulations implementing that statute,[3] and judicial decisions[4] which have interpreted it. Since the language of the indefinite escalation clause was insufficient to justify the claimed price escalation, the attempted termination of the contract was ineffectual.

It was the attempted termination under price redetermination clause which implicated the Price Protection Act, and thereby presented ERG with the opportunity to allege a constitutional violation. In dealing with this issue, the Kansas Supreme Court concluded that this redetermination clause would have authorized the escalation of the contract price up to the NGPA § 102 new gas price, but that its operation was moderated by the Price Protection Act. According to the Kansas Supreme Court, this statute limited the price escalation available to ERG under this contract to the NGPA § 109 price. In responding to ERG's constitutional attack on the Price Protection Act, the Kansas Supreme Court carefully applied the criteria established by this Court to the statute, and found it a valid exercise of the state's police power

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[2] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978).

[3] 44 F.R. 16895, CCH Vol. II § 30,040 (March 13, 1979).

[4] *Pennzoil Co. v. Federal Energy Regulatory Commission*, 645 F.2d 360, 374-75 (1981).

which was reasonable and necessary under the circumstances. In reaching this conclusion, the Kansas Supreme Court carefully reviewed and properly applied the pertinent decisions of this Court concerning the proper interpretation of the Contract Clause. Rather than attempting to sit in judgment of the wisdom of this legislation, the court below correctly applied the standard of reasonableness and necessity, and held that the Price Protection Act was well within the ambit of constitutionality established by the Contract Clause.

A. *The Price Protection Act Accomplishes an Important Social Goal.*

In passing the Price Protection Act, the Kansas Legislature was attempting to achieve three interrelated goals. It was seeking to moderate the disruptive impact the unintended and unnecessary escalation of intrastate natural gas prices, occasioned by the passage of the NGPA, would have on the Kansas intrastate gas market, and on the economy of Kansas as a whole. It was attempting to fairly apportion between suppliers and consumers the benefits and burdens of this abrupt change of intrastate gas prices. And it was attempting to provide Kansas gas users some modicum of protection from a rapid and unintended escalation of intrastate gas prices which could have resulted from the sudden shift in federal energy policy caused by the NGPA.

The need for this action was clear, and its cause can be directly traced to the passage of the NGPA. Prior to the NGPA, there were two separate gas markets; the interstate market regulated at the federal level, and the intrastate market subject to state level regulation. Pricing in the interstate gas market was controlled by the Federal Power Commission (FPC) and its successor the Federal Energy Regulatory Commission (FERC). Although the procedure used to set these interstate gas prices evolved over time, the wellhead price for inter-

state gas increased in a slow, incremental fashion.[5] In the intrastate market, gas prices were left largely unregulated by the states. The reason for this absence of state level price control legislation was the fact that the interstate gas pricing mechanism, which served to restrain interstate gas prices, also restrained intrastate gas prices. The just and reasonable area rates set for interstate gas served as a benchmark against which both the buyer and seller would measure the price of intrastate gas. Also, operation of indefinite price escalation clauses further served to link the prices paid for interstate and intrastate gas. These two factors tended to discourage inordinate increases in intrastate gas prices, and made state level regulation unnecessary.

The effect of the passage of the NGPA on the intrastate gas market was immediate and dramatic. For the first time, it created a nationwide market for all gas by establishing ceiling prices for all categories of gas. Further, it obliterated the prior interstate pricing mechanism which had served to restrain price increases in both the interstate and intrastate gas markets. This meant that subsequent to the passage of the NGPA,

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[5] Under the Natural Gas Act of 1938, the Federal Power Commission (FPC), and its successor, the Federal Energy Regulatory Commission (FERC), were given the authority to regulate all sales of gas for resale made by interstate pipeline companies. 15 U.S.C. § 717 (1976). The *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672, 982 L.Ed. 1035 (1954) decision expanded this authority to include the regulation of the wellhead price of gas sold to interstate pipelines. Subsequently, the FPC exercised complete control over the interstate gas market, but had no jurisdiction over the intrastate gas market, nor over the wellhead price of intrastate gas.

Initially, wellhead prices were set on a producer-by-producer basis. When this approach proved unwieldy, the FPC began setting wellhead gas rates on the basis of production areas. Each production area was given a just and reasonable area rate based upon the cost of producing the gas, and a reasonable return for the producers. *See Permian Basin Area Rate Cases*, 390 U.S. 747 (1968). Under this system, the wellhead price of interstate gas rose very slowly.

states could no longer rely on the restraining influence of federal regulation of interstate gas prices to hold intrastate gas prices down. And finally, the NGPA mandated rapid and constant gas price escalation by establishing artificially high ceiling prices, through political compromise, which were unrelated to any cost of production, and by building into the pricing scheme an escalation mechanism to reflect inflation which will ensure that prices will continue to spiral upwards until partial price deregulation is implemented in January, 1985. In short, the passage of the NGPA had a substantial effect on the way both interstate and intrastate gas will be priced in the immediate future.

As recognized by Congress [6] and the Kansas Legislature,[7] the effect of the passage of the NGPA on existing intrastate gas contracts containing indefinite price escalation clauses was equally dramatic. Under the terms of § 105(b)(1) of the NGPA, an existing intrastate gas contract containing a sufficient indefinite price escalation clause could result in a producers collecting the NGPA § 102 price, which had been intentionally set at a high level to encourage increased exploration and supplies for new gas, for old intrastate gas already under production. Such a result was recognized as being contrary to the basic purpose of the NGPA of increasing supplies of new gas through incentive pricing and disruptive to the state economies of gas producing states such as Kansas.

This led Congress to include in the NGPA § 602(a), 15 U.S.C. § 3432(a), which preserves to these specially

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[6] Since this problem was recognized even by the supporters of deregulation, Congress addressed it by the inclusion of § 602 in the final draft of the NGPA. *See, Proposed National Energy Plan, Hearings Before the Subcomm. on Oversight and Investigations of the House Comm. on Interstate and Foreign Commerce*, 95th Cong., 1st Sess. 6, note 23, at 119, 127, 486 (1977) (Statements of Sens. Bensten, Jackson and Gov. Briscoe).

[7] *See*, Report of the Special Committee on Energy and Natural Resources, J.S. App. at 18.

effected gas producing states the power to "establish or enforce any maximum lawful price for the first sale of natural gas produced in [the] state." This provision is explicit recognition by Congress of the need to allow gas producing states to moderate the effects of the passage of the NGPA on existing intrastate contracts to protect the economies of these states from the severe dislocation the unintended escalation of old intrastate gas prices would entail. It was considered crucial that gas producing states, whose economies are heavily dependent upon natural gas as a primary energy source, be permitted to take the corrective steps they found necessary to ensure that this shift in federal policy did not cause unintended results.

As the court below noted, the Kansas Legislature clearly saw the need for legislative action to prevent this shift in federal energy policy from having unintended and drastic effects on the economy of the state. As the special Committee on Energy and Natural Resources stated:

> The NGPA of 1978 marked a radical reversal of the federal policy toward the pricing of natural gas.
>
> . . .
>
> However, as a result of this legislation, many producers of natural gas, especially those whose contracts contain indefinite price escalation clauses, will reap unanticipated, windfall financial benefits. These benefits bear no real relationship to the costs of production of new gas, and are even more remotely related to old gas production costs. They accrue solely because of the reversal of federal policy. It is clear that the burden of the increased gas costs will be passed on by the utility companies directly to the consumer. The producers will benefit beyond any expectations they might have had only a few years ago and the consumers already buffeted by rapidly increasing inflation, including spiraling utility costs, will pay.[8]

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[8] J.S. App. at 18.

The Kansas Legislature addressed this problem in the precise manner contemplated by Congress in § 602(a) of the NGPA. It established the NGPA § 109 price as a ceiling price for old intrastate gas being sold under existing contracts containing indefinite price escalation clauses. By establishing this ceiling price, the Kansas Legislature struck a balance between the interests of the gas producers and users. This price allows gas producers to collect an escalating NGPA price for old intrastate gas, while protecting gas consumers from the economic burden of having to pay the NGPA § 102 price, a price intended for new gas, for old intrastate gas. The fact that the Price Protection Act will save Kansas gas consumers in excess of $100 million is evidence of its broad impact. Simply put, there can be no more fundamental social goal than the equitable distribution of the benefits and burdens of this major shift in federal energy policy. The economic wellbeing of a state is the most "basic interest of society." *Blaisdell*, 290 U.S. at 444-45.

ERG argues that the absence of a declared emergency is a fatal flaw in the Price Protection Act. Appellant's Brief at 28-30. This position is ill-founded. As this Court indicated in *Allied Structural v. Spannaus*, 438 U.S. 234, 249, footnote 24 (1978), a declared emergency is not a constitutional prerequisite to the exercise of the state's police power. It is simply not the case that "only an emergency of great magnitude can constitutionally justify a law impairing the obligations of contracts." States are not constitutionally required to wait until disaster has struck before they act, but are constitutionally permitted to take protective measures to ensure the public welfare when substantial economic harm is threatened.

ERG also argues that in passing the Price Protection Act, the Kansas Legislature was attempting to avert the very consequences of deregulation which Congress had deemed to be in the public interest. Appellant's Brief at 29. It is difficult to understand how the Kansas Legisla-

ture could be subverting the objectives of the NGPA by exercising the authority which that very statute granted the Legislature in the precise manner envisioned by the Congress. In discussing the purpose and intent of NGPA § 602(a) the Conference Committee stated that:

> "Congress, by adoption of this section, recognizes the right of States to prescribe more stringent limitations on the operation of such [indefinite price escalation] clauses than those prescribed herein." [9]

ERG also attempts to impugn the undeniably broad social goal of the Price Protection Act by alleging that it is not inclusive enough. Specifically, ERG alleges that only one-quarter of the gas consumed in Kansas is intrastate gas; that intrastate gas contracts with fixed price escalators are not included; that post-April, 1977, intrastate gas contracts are excluded; and that the ability to renegotiate covered contracts negates the effect of the Price Protection Act. Appellant's Brief at 30-31. These allegations stem from a basic misunderstanding of the purpose of the Price Protection Act and the limits of the state's regulatory authority.

While it is correct, as asserted by ERG, that less than one-quarter of the gas consumed in Kansas is intrastate gas, the inference which ERG draws is completely erroneous. The fact that the majority of the gas consumed in Kansas is interstate gas does not lead to the conclusion that the Price Protection Act suffers from an overly narrow focus. The Kansas Legislature has *no* authority to regulate the wellhead price of interstate gas, since that activity has been pre-empted by the federal government.[10] Rather, the Kansas Legislature has only the authority to regulate the wellhead price of intrastate gas, which is

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[9] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978).

[10] The Natural Gas Act of 1938, 15 U.S.C. § 717 (1976); The Natural Gas Policy Act of 1978, 15 U.S.C. § 3301 *et seq.* (Supp. IV 1980).

precisely what the Price Protection Act does. According to ERG, the Kansas Legislature has fallen into constitutional error for failing to exercise price control authority it constitutionally does not possess.

Careful analysis of ERG's second allegation also reveals its lack of substance. The basic purpose of the Price Protection Act was to prevent the unintended escalation of the price of intrastate gas under existing contracts by the operation of indefinite price escalator clauses due to the passage of the NGPA. The Kansas Legislature sought to protect Kansas gas users from having to pay the NGPA § 102 incentive price, intended for new gas, for old intrastate gas due to the operation of these clauses. Since existing intrastate gas contracts with fixed escalation clauses were not affected by the passage of the NGPA, and would not cause the anomalous result of producers collecting new gas prices for old intrastate gas, they were not covered by the Price Protection Act. Their inclusion was simply not needed to accomplish the goals of the Price Protection Act.

ERG's complaint that the Price Protection Act only affects contracts executed prior to April 20, 1977 also lacks substance. This was the date the National Energy Act, of which the NGPA was a part, was introduced. The Kansas Legislature logically concluded that contracts executed after that date would be drafted and executed in contemplation of the specific terms of the NGPA, while those predating the introduction of the NGPA would not. The Kansas Legislature properly exempted these contracts from the Price Protection Act provisions. Such a rational distinction does not constitute error.

Finally, ERG attempts to cast this statute as special interest legislation, designed solely for the benefit of KP&L. Appellant's Brief at 31. This argument misstates the legislative history of the Price Protection Act, and seriously misapprehends the nature of the regulatory process.

ERG alleges, with no factual support, that KP&L was the main proponent of this legislation. The facts show otherwise. The main proponent of this legislation was Governor John Carlin of Kansas, who sought to protect Kansas gas consumers, and the state's economy generally, from the disruptive effects of unintended rapid escalation of old intrastate gas being sold under existing contracts. Far from being a main proponent, KP&L was merely one of 22 witnesses which testified concerning the bill.

ERG attempts to depict KP&L as a stakeholder which will financially benefit from the Price Protection Act. Once again, the facts show otherwise. The State Commission currently has in place a purchased gas adjustment clause which permits utilities to pass on directly to their customers increases in purchased gas costs.[11] Since purchased gas is an expense which can be automatically passed on to the consumer, changes in the price of gas have *no* effect on the profitability of the utility, nor upon its earned rate of return. The utility has no direct financial stake in the price of gas it purchases.

In fact, the real stakeholders in this litigation are the gas consumers in Kansas. Had the Kansas Legislature failed to act, and allowed the price of old intrastate gas to abruptly escalate, the operation of the purchased gas adjustment clause would have passed in excess of $100 million in increased costs directly and immediately through to the consumer.[12] It is the end consumer, and not KP&L, which is the direct beneficiary of the operation of the Price Protection Act.

ERG's efforts to depict the Price Protection Act as an overly narrow piece of special interest legislation do not

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[11] State Corporation Commission of the State of Kansas, *In re General Investigation Upon the Commission's Own Motion to Establish General Policies With Regard to Purchased Natural Gas*, Docket No. 106, 850-U (April 19, 1977).

[12] Minutes of the Special Committee on Energy and Natural Resources, at 3.

withstand close scrutiny. The facts reveal, as the Kansas Supreme Court found, that this is a carefully drafted statute designed to accomplish the broad societal goal of protecting the Kansas gas consumer, and the economy of the state, from the severe dislocation it would have suffered had the price for intrastate gas being sold under existing contracts been allowed to abruptly escalate up to the new gas price level. This is precisely the type of economic legislation which is "necessary to meet an important general social problem." *Allied Structural Steel*, 438 U.S. at 247, and which this Court has routinely approved.

B. *The Price Protection Act Is A Reasonable Means of Attaining an Important Social Goal.*

This Court has consistently recognized the right of state legislatures to enact statutes which deal with important social problems, notwithstanding the fact that they may impair private contractual relationships. Such impairment does not violate the Contract Clause if the statute is "reasonable and necessary to serve an important public purpose." *United States Trust Co.*, 431 U.S. at 26. An examination of the provisions of the Price Protection Act reveal it to be just such a reasonable legislative effort.

In passing the Price Protection Act, the Kansas Legislature sought to prevent gas producers selling intrastate gas under existing contracts from reaping "unanticipated windfall benefits . . . [which] bear no real relationship to the costs of production of new gas, and are even more remotely related to old gas production costs." J.S. App. at 18. To achieve this goal, the Price Protection Act was drafted to include only those intrastate gas contracts which, due to the passage of the NGPA, would permit collection of new gas prices for old intrastate gas. This limited the scope of the Price Protection Act to those existing intrastate gas contracts containing indefinite price escalation clauses. As a consequence, the Price Pro-

tection Act affected only those contracts which were absolutely necessary to accomplish the goal of the statute.

The means chosen to accomplish this goal were also reasonable. Rather than completely freezing the price of intrastate gas sold under these contracts, or setting a price lower than was presently being paid, the Kansas Legislature established a ceiling price for this intrastate gas based upon the NGPA § 109 ceiling price. This allowed the existing intrastate gas sales contracts, including the escalation clauses, to remain in effect. It also permits the price to be paid for this gas to increase as the NGPA § 109 price escalates upwards over the life of the statute. Thus, Kansas gas producers are allowed to benefit from the passage of the NGPA by collecting the escalating NGPA § 109 price, through the continued operation of their contractual indefinite price escalation clauses. Kansas gas consumers are protected from having to pay the incentive new gas price for old intrastate gas being sold under existing contracts. In this manner, the Price Protection Act strikes a reasonable balance between the gas producer and gas consumer in the new natural gas pricing scheme established by the NGPA.

The Kansas Legislature was also aware that a state statute which conflicted with the purpose or provisions of the NGPA would be of little use, and therefore ensured that the Price Protection Act conformed to the provisions of the NGPA. The underlying purpose of the NGPA is to encourage new gas supplies by paying incentive prices for new gas. By restricting the price increases available to producers of old intrastate gas being sold under existing contracts, the Price Protection Act does not thwart the purpose of the NGPA, but is complementary to it. This is evidenced by the fact that Congress included § 602(a) in the NGPA, which specifically permits state level price regulation of intrastate gas. By doing so, Congress was not only permitting, but actually expected states

to enact lower ceiling prices for intrastate gas then under contract.

The Price Protection Act also explicitly endorsed the ceiling price concept established in the NGPA. It did so by using the NGPA § 109 price as the ceiling price for intrastate gas being sold under existing contracts containing indefinite price escalation clauses. Finally, the ceiling price so established by the Price Protection Act is scheduled to expire concurrently with the partial deregulation mandated by the NGPA.

As the Kansas Supreme Court properly determined, the Price Protection Act was a reasonable attempt by the Kansas Legislature to deal with the serious economic problem confronting this gas producing state due to the reversal of federal energy policy embodied in the NGPA. This act is only as broad as is necessary to accomplish its goal, without exceeding the authority of the state in the area of price control legislation. It strikes a reasonable balance between the understandable desire of gas producers to receive the highest possible price for old intrastate gas, and the need to protect the economy of the state from the dislocations which would be caused by an abrupt escalation of intrastate gas prices through the operation of indefinite price escalation clauses. The Price Protection Act is a carefully drawn statute which is reasonably designed to accomplish this goal.

ERG argues that this Court should apply a version of strict scrutiny to any statute which impinges upon an existing contractual relationship. Appellant's Brief at 36-41. Under this reasoning, the Court should consider whether the legislature selected the appropriate alternative in solving the problem it confronted, whether the minority or majority committee reports were more persuasive, and whether the proper economic balance was struck. ERG would have this Court undertake all of these tasks based upon a misinterpretation of this Court's holding in *United States Trust*. According to ERG, that case

warrants a judicial redetermination of the reasonableness and necessity of any statute which infringes, however remotely, on an existing contract relationship.

The *United States Trust* decision does not stand for such a proposition, but rather for two entirely different propositions. First, when a court reviews economic regulation, such as the Price Protection Act, it should defer to the legislative determination of reasonableness and necessity. As the Court stated:

> As is customary in reviewing economic and social regulation, however, courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure.[13]

And second, this deference by the Court is not appropriate if, *but only if*, the state's own self-interest is at stake. As the Court stated:

> As with laws impairing the obligations of private contracts, impairment may be constitutional if it is reasonable and necessary to serve an important public purpose. In applying this standard, however, complete deference to a legislative assessment of reasonabless and necessity is not appropriate because the State's self-interest is at stake.[14]

This longstanding rule was not abandoned by the Court in *Allied Structural Steel*, but was reaffirmed. In that case, the normal presumption favoring legislative judgment as to the reasonableness and necessity of a particular measure could not stand because there was absolutely "no showing in the record before us that this severe disruption of contractual expectations was necessary to meet an important general social problem." *Allied Structural Steel*, 438 U.S. at 244, 247. In this case, the record conclusively establishes the events which caused the Kansas Legislature to consider this legislation, the need that it addressed, and

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[13] *United States Trust Co.*, 431 U.S. at 22-23.

[14] *Id.* at 26.

the important general problem with which the Price Protection Act deals. In contrast to the *Allied Structural Steel* case, the completeness of the record makes an independent judicial determination of the reasonableness and necessity of this statute unnecessary and redundant.

The Kansas Supreme Court deferred to the legislative determination of the reasonableness and necessity of the Price Protection Act because the state's self-interest was not involved in the contract affected by the statute, and because the record before it established the general social problem with which the price protection was to deal. This approach was in complete accord with the *United States Trust* and *Allied Structural Steel* cases. Under the holdings in those cases, a judicial inquiry into the reasonableness and necessity of economic legislation is only warranted when the state acts to abrogate its own contract, or the record fails to show the problem the statute is to remedy. Such is not the case in the instant proceedings.

There are sound policy reasons why this Court has refused to substitute its judgment for that of the Legislature as to what is the wisest or best course in the area of economic legislation. The legislative branch is uniquely suited to weigh and balance competing and conflicting economic interests and theories. "[T]he place for determining their weight and significance is the legislature, not the judiciary." *East New York Savings Bank v. Hahn*, 326 U.S. 230, 234 (1935). The courts are neither suited nor equipped to make such determinations, since they involve questions of social theory, economic policy, and conflicting interests of competing groups. This Court has wisely declined to become enmeshed in attempting to sort out the proper course a legislature should have followed under a particular set of circumstances.

The inappropriateness of the course of action espoused by ERG is easily highlighted by reviewing some of the questions such an approach would pose to the Court.

Should the State Commission deny KP&L a pass-through of these higher costs? Should the legislature freeze all intrastate gas prices? Should incremental pricing be adopted? ERG seeks to fundamentally change the role of this Court from a body which considers the constitutionality of a statute to one which would second guess the wisdom of the course selected by the legislature. The Contract Clause should not be utilized as a vehicle for shifting legislative functions to the judiciary. Unfortunately, this is precisely the result of ERG's approach.

In summary, the Price Protection Act is a carefully drawn statute which affects only those contracts necessary to accomplish its important social goal of protecting Kansas gas consumers from unintended price escalation of old intrastate gas sold under existing contracts. It does not overreach the regulatory authority of the state, and comports with the regulatory purpose and scheme of the NGPA. It is the reasonable type of price control legislation to which deference is due.

C. *The Price Protection Act Imposes Only a Modest and Temporary Burden on Affected Contracts.*

The flexible standard which the Court has developed for judging the constitutionality of state legislation which affect existing contractual relations recognizes that a modest burdening of existing contracts does not offend the Contract Clause. It is therefore important to determine whether the challenged statute imposes "a substantial impairment of the contractual relationship," since a "minimal alteration of contractual obligations may end the inquiry at the first stage." *Allied Structural Steel*, 438 U.S. at 244-45.

The Price Protection Act imposes only a modest burden on the contracts affected by it. Contrary to the assertions of ERG, the Price Protection Act does not render inoperative the central term of the contract. Rather, this statute merely moderates the operation of the

indefinite price escalation clauses in a reasonable fashion. Instead of allowing gas producers to collect the NGPA § 102 price, intended as an incentive price for new gas, it allows them to collect the NGPA § 109 price. The indefinite price escalation clauses continue to operate, and to allow producers to collect higher prices as the NGPA § 109 price escalates. The central pricing term of the contracts are left unaffected by the Price Protection Act, and only the operation of the contingent indefinite price escalation clauses is moderated.

Two other facts strongly indicate that the impairment imposed on ERG by the Price Protection Act is minimal. First, the escalation clauses contained in the contract are specifically made subject to "all relevant present and future state and Federal laws." Since ERG voluntarily made the terms of the contract, including both price escalation clauses, subject to future state laws such as the Price Protection Act, it should not be heard to complain that its contractual relationship is burdened by the passage of just such a statute to which the contract is made subject. One federal district court has already held the presence of such a clause vitiates any claim of an impairment sufficient to sustain a Contract Clause violation.[15]

Second, the very statute upon which ERG relies specifically authorizes the type of intrastate gas price control legislation passed by the Kansas Legislature. Congress foresaw that the passage of the NGPA would cause a quantum leap in intrastate gas prices, far exceeding the expectations of the parties, due to the operation of indefinite price escalation clauses. Knowing that this would disastrously disrupt the economies of gas producing states such as Kansas, Congress specifically gave

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[15] *Edmiston v. State Corporation Commission*, No. 79-1335 (D. Kan., Nov. 24, 1980), *modified* (D. Kan., Jan. 13, 1981), *appeal docketed* No. 71-1197 (10th Cir. Feb. 23, 1981).

these states authorization in the NGPA to deal with these problems. Section 602(a) of the NGPA states:

> Nothing in this Act shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such state which does not exceed the applicable maximum lawful price, if any, under Title I of this Act.

The intent of this provision was explained by the Joint Explanatory Statement of the Committee on Conference, where it is said:

> The conference agreement provides that nothing in this Act shall affect the authority of any state to establish or enforce any maximum lawful price for the sales of gas in intrastate commerce which does not exceed the applicable lawful price, if any, under Title I of this Act. *This authority extends to the operation of any indefinite price escalator clause.* (Emphasis supplied.) [16]

In passing the Price Protection Act, the Kansas Legislature was exercising its police power to reapportion the economic dislocation caused by the passage of the NGPA, just as Congress authorized in § 602(a) of the NGPA. ERG should not be heard to complain that its right to a higher contract price under the NGPA has been infringed by the Price Protection Act, when the very statute upon which ERG relies authorizes just such a limitation. This is particularly true when it is remembered that even the modest restriction placed on the operation of these indefinite price escalation clauses ceases, under the terms of the Price Protection Act, in December, 1984.

Reduced to its essence, ERG's impairment argument is really a complaint that it is not receiving new gas prices for old intrastate gas, and that the size of the windfall it is receiving due to the passage of the NGPA is not sufficiently large. This is hardly the type of "substantial

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[16] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess., 124-25 (1978).

impairment of a contractual relationship" which would offend the Contract Clause. *Allied Structural Steel*, 438 U.S. at 244. Rather, the Price Protection Act is a moderate statute which operates to "restrict a party to those gains reasonably expected from the contract," and is "not subject to attack under the Contract Clause." *El Paso*, 397 U.S. at 515.

D. *Summary.*

The Price Protection Act is a reasonable and carefully drawn statute which seeks to protect Kansas from the unintended effects of an abrupt change in federal energy policy. It accomplishes this important social goal in a manner expressly authorized by Congress, and in a way which does not eliminate but merely limits the size of the unintended windfall the passage of the NGPA generated for intrastate gas producers. In judging the constitutionality of this statute, it is well to remember that "one whose rights, such as they are, are subject to state restriction, cannot remove them from the power of the state by making a contract about them." *Hudson Water Co. v. McCarter*, 209 U.S. 349, 357 (1908).

II. The Kansas Supreme Court Properly Interpreted NGPA § 105(b)(1).

It has been recognized by Congress,[17] the FERC[18] and the Fifth Circuit Court of Appeals[19] that the escalation of the price of gas under existing intrastate gas contracts is controlled by the express terms of the contract. In analyzing the language contained in the ERG contract to determine whether price escalation was authorized, the Kansas Supreme Court went through a two-step anal-

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[17] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978).

[18] 44 F.R. 16895, CCH Vol. II § 30,040 (March 13, 1979).

[19] *Pennzoil Co. v. Federal Energy Regulatory Commission*, 645 F.2d 360, 374-75 (1981).

ysis. First, it reviewed the operation of the NGPA, and specifically § 105(b)(1). Relying upon the Fifth Circuit interpretation of that section contained in *Pennzoil Co. v. Federal Energy Regulatory Commission*, 645 F.2d 360, (1981) the court determined that if the price under the contract on November 9th was less than the NGPA § 102 price, the price could escalate up to the NGPA § 102 price so long as the contract contains a sufficient escalation mechanism.

Next, turning to the language of the contract itself, the Kansas Supreme Court concluded:

> We hold that under the terms of the government price escalator clause in these contracts, and under the applicable section of the NGPA, the November 9th gas price (which was lower than the Section 102 price) did not escalate . . . . The NGPA did not trigger a price increase because the contracts herein did not contain a sufficient escalation mechanism.[20]

Under the Kansas Supreme Court's analysis, the mere establishment of ceiling prices due to the passage of the NGPA did not trigger the escalation clause as claimed by ERG. It concluded that under the facts and circumstances of this case, the words of the contractual escalation clause did not authorize the collection of the higher price claimed by ERG. As a consequence, the attempted termination of the contract by ERG was ineffectual.

The fact that the Kansas Supreme Court clearly understood and properly applied § 105(b)(1) of the NGPA was reemphasized in the clarifying opinion rendered in *Mesa Petroleum v. The Kansas Power and Light Co.*, 229 Kan. 631, 629 P.2d 190, *clarified* 230 Kan. 166, 630 P.2d 1129 (1981), *cert. denied*, 50 U.S.L.W. 3592 (U.S. Jan. 25, 1982) (No. 81-711), which was issued the same day as the decision in this case. In that case, the Kansas Supreme Court stated:

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[20] J.S. App. at 15a.

> As we interpret the N.G.P. Act it does not preclude escalation of prices under contract clauses up to N.G.P. Act ceiling prices. On the other hand, contrary to the assumption of *Mesa*, the mere enactment of the N.G.P. Act did not activate price escalation clauses, such as the one in the present case, so as to escalate prices to the N.G.P. Act ceiling level.

This analysis of § 105(b)(1) of the NGPA, and its application to the escalation clause contained in this contract, conforms with the intent of Congress in passing the NGPA. As stated in the Joint Explanatory Statement:

> Some intrastate contracts currently in existence contain indefinite price escalator clauses which can be triggered by a number of factors, including adjustments by the Commission of "just and reasonable" rates established under the Natural Gas Act. *The conferees do not intend that the mere establishment of the ceiling prices under this Act shall trigger indefinite price escalator clauses in existing intrastate contracts.* (Emphasis supplied).[21]

This case presented the Kansas Supreme Court with a question of the interpretation of the meaning and operation of specific contractual terms contained in an intrastate gas supply contract. The Kansas Supreme Court interpreted that contract as not authorizing price escalation, and did so in conformity with the meaning and intent of § 105(b)(1) of the NGPA. ERG's attempts to portray this decision as being in conflict with § 105(b)(1) of the NGPA are without merit and should be rejected.

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[21] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 83 (1978).

CONCLUSION

For the foregoing reasons, the Court should sustain the decision of the Kansas Supreme Court holding the Price Protection Act constitutional in all respects.

Respectfully submitted,

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No. 81-1370

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

ENERGY RESERVES GROUP, INC., *Appellant,*

—v.—

THE KANSAS POWER AND LIGHT COMPANY, *Appellee.*

ON APPEAL FROM THE SUPREME COURT OF KANSAS

BRIEF *AMICUS CURIAE* OF OKLAHOMA NATURAL GAS COMPANY, OKLAHOMA GAS AND ELECTRIC COMPANY, PUBLIC SERVICE COMPANY OF OKLAHOMA, AND THE OKLAHOMA ASSOCIATION OF ELECTRIC COOPERATIVES

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No. 81-1370

ENERGY RESERVES GROUP, INC.,

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Appellee.

ON APPEAL FROM THE SUPREME COURT OF KANSAS

BRIEF *AMICUS CURIAE* OF OKLAHOMA NATURAL GAS COMPANY, OKLAHOMA GAS AND ELECTRIC COMPANY, PUBLIC SERVICE COMPANY OF OKLAHOMA, AND THE OKLAHOMA ASSOCIATION OF ELECTRIC COOPERATIVES

STATEMENT OF INTEREST OF *AMICI CURIAE*[1]

Oklahoma Natural Gas Company, Oklahoma Gas and Electric Company, Public Service Company of Oklahoma, and the Oklahoma Association of Electric Cooperatives ("Oklahoma Natural *et al.*") are three major Oklahoma public utilities and one association of Oklahoma electric cooperatives.[2] Each of

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1 The parties have consented to the filing of this brief.

2 Oklahoma Natural Gas Company supplies natural gas to customers in an area comprising two-thirds of Oklahoma. It had in excess of 500,000 residential, 50,000 commercial, 2,400 industrial and 50 wholesale customers

these corporations (or its members) purchases substantial volumes of natural gas in the Oklahoma intrastate market, or purchases electricity generated from natural gas.

Oklahoma Natural *et al.* have an interest in this case because they operate under an Oklahoma statute similar to the Kansas statute involved in this appeal. Specifically, the Oklahoma Natural Gas Price Protection Act, enacted on March 19, 1979, limits the effect of indefinite price escalator clauses found in most long-term gas purchase contracts between purchasers and producers of Oklahoma intrastate natural gas. OKLA. STAT. tit. 52, §§ 260.1-260.13 (1981) ("OKLA. § __"). The Kansas statute, which was enacted in May 1979, was largely copied from the Oklahoma statute, as indicated in Appendix A hereto.

Litigation challenging the validity of the Oklahoma statute is pending in the United States District Court for the Western District of Oklahoma. (*Energy Consumers and Producers Association, et al.* v. *Baker,* W.D. Okla., Civ. Nos. 79-320-D & 79-823-D.) Plaintiffs in that litigation—including Amerada Hess Corporation and two major trade associations that represent over 1500 producers of natural gas—contend that the Oklahoma statute violates the Contract Clause of the United States Constitution (Const. Art. I, § 10). Oklahoma Natural Gas Company and the Oklahoma Association of Electric Cooperatives intervened as defendants in that action. A decision on the issues presented herein has not yet been rendered by the district court in the Oklahoma case.

In Oklahoma, increases in the cost of intrastate natural gas purchased by Oklahoma Natural *et al.* are passed on directly to their customers pursuant to Oklahoma law and the terms of

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in its fiscal year ended August 31, 1979. (This data is contained in a stipulation filed on March 24, 1980 by all parties in *Energy Consumers & Producers Ass'n* v. *Baker,* W.D. Okla., Civ. Nos. 79-320-D & 79-823-D, ¶ 3(b)(i) [hereinafter Okla. Stip.].) Oklahoma Gas and Electric Company and Public Service Company of Oklahoma are electric utilities that generate power by using natural gas; they served approximately 800,000 residential users and 117,000 commercial and other users in Oklahoma in 1979. *Id.* ¶¶ 22(a), 23(a). The members of the Oklahoma Association of Electric Cooperatives serve approximately 250,000 residential users.

purchased gas adjustment clauses in utility tariffs, which operate as authorized by the Oklahoma Corporation Commission. OKLA. STAT. tit. 17, §§ 250-264 (1981).[3] Thus, if the Oklahoma Natural Gas Price Protection Act were held to violate the Contract Clause, the cost of natural gas to Oklahoma Natural *et al.*—and to the hundreds of thousands of customers they serve—would increase substantially.

This Court's decision may be dispositive of, and certainly will have a significant bearing on, the Oklahoma litigation. Although the forensic approach of appellant is to focus its arguments on alleged peculiarities concerning the manner in which the Kansas statute was enacted, clearly the resolution of its constitutional claims will have a broader impact.[4] It is thus important that this case be decided with a full appreciation of all the state statutes that will be affected.

STATEMENT OF FACTS

The Kansas Natural Gas Price Protection Act, KAN. STAT. ANN. §§ 55-1401—55-1415 (Supp. 1981) ("KAN. § __"), and the Oklahoma Natural Gas Price Protection Act, OKLA. §§ 260.1-260.13, were enacted against the backdrop of extensive prior regulation of the natural gas industry at the state and federal levels, and, in particular, were a direct outgrowth of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3432 (Supp. IV 1980) ("NGPA").[5]

Because this case depends upon an understanding of the historical development of and the interplay between federal and state price regulation of the natural gas industry, and because appellant's brief contains an incomplete and mislead-

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3 Okla. Stip. ¶¶ 3(b)(ii), 22(b), 23(b).

4 Appellant claimed in its Jurisdictional Statement that review by this Court of the Kansas case would "give needed guidance" to the lower courts in the Oklahoma litigation. (J.S. 25 n.37.)

5 The Oklahoma and Kansas statutes will be referred to herein as the "State Price Protection Acts."

ing picture of Congress' intent in enacting the NGPA, we begin with an overview of the relevant statutes. This review not only demonstrates that the natural gas industry and the use of indefinite price escalator clauses in that industry have traditionally been regulated in the public interest; it also shows that Congress specifically intended in the NGPA to "cede" to the states the power to restrict "the operation of any indefinite price escalator clause" in intrastate contracts. S. REP. NO. 1126, 95th Cong., 2d Sess. 83, 124-25 (1978).

1. State and Federal Legislation Prior to the NGPA

The production and sale of natural gas have been regulated by Oklahoma and Kansas since early in this century. In Oklahoma, a comprehensive law was enacted in 1913 that required gas pipelines to purchase ratably and without discrimination from all producers; prohibited waste; defined rights of ownership; provided for unitized management of common sources of gas; and conferred on the state Corporation Commission the power to fix the price of gas produced from a common source where the owners could not agree. *See* OKLA. STAT. tit. 52, §§ 23-24, 29, 231-33, 236-40, 243, 477 (1981). Subsequent legislatures have supplemented and refined this system of regulation. In Kansas, legislation designed to provide for orderly production and to prevent waste of natural gas has also existed for many decades. KAN. STAT. ANN. §§ 55-701 *et seq.* (1976 & Supp. 1981).

At the federal level, Congress enacted the Natural Gas Act in 1938, 15 U.S.C. §§ 717-717w (1976). Congress declared that "the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest," 15 U.S.C. § 717(a), and it therefore authorized the Federal Power Commission ("FPC") to regulate the "rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission . . . ." 15 U.S.C. § 717c(a). The Natural Gas Act did not apply to wholly intrastate transactions, because Congress be-

lieved in 1938 that such sales were "matters primarily of local concern and subject to regulation by the several States." 15 U.S.C. § 717(c).

This Court held in 1954 that the FPC's jurisdiction extended to wellhead prices for natural gas sold in interstate commerce, *Phillips Petroleum Co.* v. *Wisconsin,* 347 U.S. 672, and the FPC thereafter established a comprehensive system for regulating those prices.[6] A particular object of this regulation was indefinite price escalator clauses, which the FPC found generally "contrary to the public interest." *See* pp. 16-17, *infra.*

2. The NGPA

The NGPA, which became effective in December 1978, substantially altered the Natural Gas Act's regulatory regime. The NGPA established a ceiling price for various categories of natural gas and provided for monthly upward price adjustments for each such category during the period from December 1978 to December 1984, based on an "inflation adjustment factor" and other considerations.[7] Thereafter, the NGPA provided for the deregulation of the prices of many categories of natural gas commencing January 1, 1985. 15 U.S.C. § 3331. In addition, in the NGPA, Congress regulated to a limited extent the wellhead price of natural gas that was not sold in interstate commerce, and expressly delegated to the states the power to adopt more comprehensive statutes governing these intrastate sales.

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6 Under the Natural Gas Act after 1954, producers of gas for the interstate market were subject to a new regime of economic regulation that overrode existing contracts in several ways. For example, at the time of the *Phillips* decision many preexisting contracts contained automatic price redetermination clauses, and these provisions became ineffective under the Act. *See, e.g., Bel Oil Corp.* v. *FPC,* 255 F.2d 548, 554 (5th Cir.), *cert. denied,* 358 U.S. 804 (1958); *Cities Service Gas Producing Co.* v. *FPC,* 233 F.2d 726, 730 (10th Cir.), *cert. denied,* 352 U.S. 911 (1956).

7 *See, e.g.,* 15 U.S.C. §§ 3312(b), 3314(b), 3315(b), 3319(b).

(a) NGPA Price Regulation for "New" Gas and for "Old" Interstate Gas

The NGPA permits higher prices for some categories of gas than for others. In § 102 of the NGPA (reproduced in Appendix B), Congress attempted to encourage new exploration and drilling by allowing high, incentive prices for "new" gas.[8] The § 102 new-gas price as of December 1978 was $2.078 per million Btu's (MMBtu),[9] and this price rises each month on the basis of an "inflation adjustment factor" plus an additional 3.5 or 4 percent annualized upward adjustment.[10]

At the other end of the spectrum, § 104 of the NGPA (reproduced in Appendix B) retains the preexisting schedule of maximum wellhead prices for "old" interstate gas, based on the drilling date of the well from which the gas was produced.[11] These "old" gas prices, as of December 1978, ranged from $0.332 per MMBtu for large producers in the case of interstate gas from wells drilled prior to January 1973 to $1.63 per MMBtu in the case of wells drilled after January 1, 1975. (*See* Appendix C hereto). The natural gas involved in this case (and in the Oklahoma case) is "old" intrastate gas.[12] Thus, if the

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8 Section 2(3) of the NGPA, 15 U.S.C. § 3301(3), defines the term "new well" as one "the surface drilling of which began on or after February 19, 1977" or "the depth of which was increased, by means of drilling on or after February 19, 1977" by at least 1000 feet. Section 102(c), in turn, defines the term "new gas" as natural gas produced from certain kinds of "new wells" or from new reservoirs of natural gas.

9 The term "Btu" (British thermal unit) refers to the energy value of natural gas. "MMBtu" means one million Btu's. The term "Mcf" means one thousand cubic feet of gas. Roughly, one Mcf equals one MMBtu.

10 The NGPA also provides high incentive prices for so-called "high cost" natural gas (*i.e.*, from certain deep wells) and "stripper well" gas (*i.e.*, from low-production wells). NGPA §§ 107 & 108, 15 U.S.C. §§ 3317 & 3318.

11 The term "old gas" is not defined as such in the NGPA. The term "old well" is defined as any well other than a "new well." 15 U.S.C. § 3301(4).

12 Neither the Oklahoma nor the Kansas statute regulates the price of "new" gas. Thus, to the extent that appellant or other gas producers are

contracts at issue had involved sales across a state line, the prices would be constrained by NGPA § 104—a section of the statute never mentioned in appellant's brief.

The congressional rationale for distinguishing between "old" and "new" gas for pricing purposes was that high, incentive prices were desirable in order to encourage development of new energy resources. Congress in 1978 recognized that this rationale did not apply to wells that had already been drilled in the 1950s, 1960s, or in the 1970s prior to 1977. The regulated prices that were available to the producers at those earlier times obviously were sufficient to encourage investment in those wells, and were deemed to be compensatory and fair. Congress concluded that if the price of this "old" gas were deregulated, producers would receive a windfall without stimulating new drilling.

In addition to the § 102 new-gas price and the § 104 interstate old-gas price, the ceiling price established by § 109 of the NGPA is important in this case. This is because the Oklahoma and Kansas statutes use the § 109 price, rather than the § 104 price or the § 102 price, as the reference point in regulating the price of "old" intrastate gas. Section 109 is a catch-all provision that applies to natural gas not covered by other sections of the NGPA. The § 109 price was established by Congress at a level equal to the *highest* price of "old" natural gas in the interstate market. The § 109 price escalates each month on the basis of the same "inflation adjustment factor" applicable to other categories of natural gas.

Appendix C sets forth and compares, for each month from December 1978 to the present, the maximum prices allowed for various categories of natural gas under §§ 102, 104 and 109 of the NGPA, as well as the prices actually being paid by Oklahoma Natural under its existing intrastate contracts during the same period of time. This Appendix shows (i) that while the § 109 price is less than the § 102 new-gas price, it is well above the maximum allowable price for most categories of "old"

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selling "new" gas in interstate or intrastate commerce, they are eligible to receive the NGPA "new" gas prices.

interstate gas; (ii) that in December 1978 the § 109 price was approximately the same as the highest price being paid by Oklahoma Natural under *any* of its unregulated intrastate contracts, and (iii) that in December 1978 the prices being paid in the Oklahoma intrastate market were well below the § 102 new-gas price.

(b) NGPA Price Regulation for "Old" Intrastate Gas Sold Pursuant to an Existing Contract

Congress provided in the NGPA for partial federal regulation of the wellhead price of natural gas sold to intrastate users. The various pricing provisions of the NGPA relating to "new gas" (§ 102), "high-cost" gas (§ 107), and "stripper well gas" (§ 108) apply to intrastate, as well as interstate, gas in those categories. With respect to "*old*" intrastate gas covered by a preexisting contract, § 105 of the NGPA is applicable. The contracts involved in this litigation are all covered by NGPA § 105.

Section 105 provides that the maximum price for the first sale of intrastate gas covered by contracts that were in existence as of November 8, 1978 shall be the lower of the contract price or the § 102 new-gas price. In an intrastate contract containing an indefinite price escalator clause, the contract price would ordinarily escalate to the § 102 price;[13] thus, the § 102 new-gas price would be permissible as far as federal law was concerned. Accordingly, *in the absence of supplemental legislation at the state level*, § 105 would have permitted prices for "old" gas under existing, intrastate contracts to escalate to the high, incentive price authorized by NGPA § 102 for "new" gas.

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13 Under most intrastate contracts, natural gas was being sold at a price below the § 102 new-gas price at the time the NGPA was enacted. However, the typical Oklahoma intrastate contract contains an indefinite price escalator clause that would be triggered by higher prices being paid by other purchasers for either "new" or "old" gas. Accordingly, as soon as Oklahoma purchasers started buying "new" gas at the § 102 price, the escalator clauses would cause the "contract price" to escalate to the § 102 price.

However, of critical importance to this case is § 602(a) of the NGPA. There, Congress made clear that it did not intend to give gas producers a federal statutory *right* to receive new-gas prices for "old" intrastate gas; rather, it simply established the § 102 price as an absolute federal limit on price escalations and expressly authorized the states to impose additional, more stringent restrictions on the effect of indefinite price escalator clauses in intrastate contracts. Section 602(a) provides:

> Nothing in this chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under subchapter I of this Act.

In the Conference Committee Report that accompanied the NGPA, the Senate and House conferees left no doubt that the purpose of § 602 was to delegate to the states the authority to enact legislation restricting the effect of indefinite price escalator clauses in intrastate contracts. The conferees emphasized:

> that nothing in this Act shall affect the authority of any State to establish or enforce any maximum lawful price for sales of gas in intrastate commerce which does not exceed the applicable maximum lawful price, if any, under Title I of this Act. This authority extends to the operation of any indefinite price escalator clause. The Congress enacts this provision with a recognition that it is ceding its authority under the commerce clause of the Constitution to regulate prices for such production to affected States.[14]

Likewise, in explaining § 105 of the NGPA (which, standing alone, would permit indefinite price escalator clauses in intrastate contracts to operate up to the § 102 new-gas price), the conferees noted:

> The conference agreement specifically prohibits prices paid in any sale of high-cost natural gas [§ 107 gas] from

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14 S. Rep. No. 1126, 95th Cong., 2d Sess. 124-25 (1978); H.R. Rep. No. 1752, 95th Cong., 2d Sess. 124-25 (1978).

> triggering the operation of any indefinite price escalator clauses. [*See* NGPA § 313.] *The conference agreement also cedes the Federal Government's authority to further limit the operation of indefinite price escalator clauses to State governments wishing to do so. The Congress, by adoption of this section, recognizes the right of States to prescribe more stringent limitations on the operation of such clauses than those prescribed herein.*

Id. at 83 (emphasis added).[15] The State Price Protection Acts are a direct outgrowth of this delegation of authority.[16]

3. The State Price Protection Acts

The State Price Protection Acts are consistent with, and simply complement, the NGPA. The scope of both statutes is carefully limited to the particular regulatory gap in the NGPA that Congress expressly reserved for regulation by the states—namely, *intrastate* contracts covering "*old*" gas. And with respect to this one category of gas, the State Price Protection Acts simply prohibit the taking into account, "in applying any indefinite price escalator clause contained in any gas purchase contract subject to this act," the "price allowed to be paid

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15 *See also Natural Gas Pricing Agreement Adopted by the Conferees on H.R. 5289*, 95th Cong., 2d Sess. 19 (Comm. Print 1978).

16 In view of the express delegation of federal power in § 602, and the fact that the Oklahoma and Kansas legislation simply parallel at the state level what Congress did in the NGPA for interstate gas, it is questionable whether this case should be decided under legal standards that are any different than those applied when federal economic-regulatory legislation is attacked under the Due Process Clause. The Oklahoma and Kansas statutes were enacted as part of the overall regulatory scheme established by Congress pursuant to *federal* power under the Commerce Clause of the Constitution. As appellant concedes (Appt's Br. 40-41 n.55), federal legislation under the Commerce Clause must be upheld unless there is "no reasonable connection between the regulatory means selected and the asserted ends." However, since the Oklahoma and Kansas statutes easily satisfy all of the criteria established by this Court under the Contract Clause, we will assume for purposes of this brief that Contract Clause principles are controlling.

pursuant to federal legislation" and the prices paid by other intrastate purchasers of gas, to the extent that such reference prices would produce a contract price in excess of the NGPA § 109 price. OKLA. §§ 260.4 & 260.5; KAN. §§ 55-1404 & 55-1405. (Reproduced in Appendix A.)

By using the NGPA § 109 price as their reference price, the Oklahoma and Kansas statutes permit generally *higher* prices to be paid to producers than would be permitted under § 104 of the NGPA for interstate sales of the same gas. (*See* Appendix C.) Moreover, the narrow prohibition of the State Price Protection Acts is subject to a number of exemptions designed to prevent the statutes from operating in an area broader than the regulatory field reserved to the states by Congress in the NGPA. The Oklahoma and Kansas statutes define the terms "new well," "new reservoir" and "stripper well" identically with the definitions of these terms in the NGPA,[17] and both statutes permit producers to receive the same prices for gas produced from such wells as they would receive under the NGPA.[18] The State Price Protection Acts also exempt indefinite escalator clauses in contracts dated on or after April 20, 1977[19]—the date of President Carter's announcement of his new energy policy that led to the NGPA. 13 *Weekly Comp. Pres. Doc.* 566 (April 20, 1977). Thus, to the extent that private contracts were made in reliance on the new policy although prior to the NGPA, such contracts are not affected. Moreover, both of the state statutes contain an "anti-rollback" provision that protects producers against any reduction in the prices that were actually being paid prior to enactment of the state statutes.[20] And both statutes expire on December 31,

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17 *Compare* NGPA §§ 102(c)(1)(B) & (C), 108(b), 15 U.S.C. §§ 3312(c)(1)(B) & (C), 3318(b), *with* KAN. § 55-1402(d), (e) & (f), *and* OKLA. § 260.2(4), (5) & (6).

18 KAN. § 55-1406; OKLA. § 260.6.

19 KAN. § 55-1403; OKLA. § 260.3.

20 KAN. § 55-1404; OKLA. § 260.4.

1984, simultaneously with the expiration of price controls on many categories of natural gas under the NGPA.[21]

In the absence of this state legislation, prices for "old" gas under intrastate contracts would have shot up to the maximum prices permitted for "new" gas under § 102 of the NGPA. In December 1978 the *highest* price being paid by Oklahoma Natural under any intrastate contract, net of severance taxes, was $1.645 per Mcf. The § 102 new-gas price for the same month was $2.078. (*See* Appendix C.) Thus, if the indefinite price escalator clauses had been permitted to operate, the producer-sellers in Oklahoma would have received an immediate, windfall price increase of 26 percent, over and above the increase of several hundred percent that had occurred in recent years.[22] The Oklahoma and Kansas Price Protection Acts prevented these sudden price escalations from occurring, and eliminated the anomalous result of treating "old" gas as if it were produced from a "new" well for which a substantial investment had freshly been made, while permitting producers to receive a price at least as high as that permitted by Congress for similar gas sold across a state line.

SUMMARY OF ARGUMENT

I. The State Price Protection Acts constitute a reasonable and appropriate response to a serious matter affecting the public interest, and are lawful under the Contract Clause.

II. The public interest in regulating inflationary increases in energy prices cannot be seriously questioned. Natural gas is an essential resource, and its price affects every citizen. Energy prices rose dramatically during the 1970s, causing shock effects to be felt throughout the economy. The impact on consumers

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21 KAN. § 55-1411; OKLA. § 260.13.

22 In January 1972 the average price being paid by Oklahoma Natural for intrastate gas was $0.209 per Mcf, including severance taxes. This price had risen to $1.454 by January 1979—an increase of approximately 700% in seven years. Okla. Stip. ¶ 7.

has been particularly severe. Because of its importance, regulation as to price and supply of natural gas has existed for many years.

The contractual provision at issue—the indefinite price escalator clause—is an especially appropriate subject of regulation. Such clauses exacerbate inflation by causing prices in a multitude of contracts to escalate quickly to the highest prices being paid in a wide geographical area. The Federal Power Commission limited such clauses in interstate contracts twenty years ago, and this Court acknowledged some fourteen years ago that the government has a legitimate interest in restricting them.

The public interest benefits of the Oklahoma and Kansas Natural Gas Price Protection Acts are substantial. In Oklahoma, consumers will save hundreds of millions of dollars between 1979 and 1984 as a result of the statute. Under Oklahoma law, consumers directly receive the benefits of the savings by Oklahoma Natural *et al.* in their natural gas purchase costs. Under the established precedents of this Court, remedial legislation of the kind involved in this case does not violate the Contract Clause of the Constitution, notwithstanding that such legislation may affect preexisting contracts.

III. The State Price Protection Acts are not impermissibly narrow. Both statutes were carefully drafted so as to fill the particular regulatory gap in the NGPA that Congress left to further regulation by the states. Moreover, it is well-established that the constitutionality of state regulatory statutes does not depend on whether a broader statute might have been more effective than the solution adopted by the legislature. Furthermore, the suggestion of appellant that consumers could have been protected in an alternative way—by permitting the producing interests to receive hundreds of millions of dollars in price escalations, but requiring public utilities and cooperatives to absorb these massive increases without passing them on to their customers—is totally unrealistic, and its implementation would be unlawful.

IV. The Acts do not substantially impair the obligations of contracts. They do not require any reduction in prices actually

paid prior to their effective dates, and, to the extent contractually provided, they permit the same gradual price increases as are permitted under § 109 of the federal statute. The sole effect of the statutes is to prevent windfall price increases that the producers have no constitutionally protected right to receive. Moreover, the state statutes are temporary in duration.

ARGUMENT

I. INTRODUCTION

Although Article 1, § 10 of the Constitution literally prohibits the states from enacting "any" law impairing the obligations of contracts, it has long been clear that "the prohibition is not an absolute one and is not to be read with literal exactness like a mathematical formula." *Home Building & Loan Association* v. *Blaisdell,* 290 U.S. 398, 428 (1934). It is a basic "postulate of the legal order" that the states retain the power to legislate in the public interest even though some private contract rights will be affected. *Id.* at 435. *Accord, e.g, East New York Savings Bank* v. *Hahn,* 326 U.S. 230, 232 (1945). The authority of the state is not narrowly limited to matters affecting health, morals and safety: "It extends to economic needs as well." *Veix* v. *Sixth Ward Building & Loan Association,* 310 U.S. 32, 37-39 (1940). *See also City of El Paso* v. *Simmons,* 379 U.S. 497, 506-07 n.9, 508 (1965).

A rule of reason must thus be applied in cases arising under the Contract Clause. *See, e.g., United States Trust Co.* v. *New Jersey,* 431 U.S. 1, 22 (1977). On the one hand, the reserved power of the states cannot be construed to permit the adoption of a policy favoring the repudiation of debts; on the other, the Clause is not to be construed to prevent the states from dealing with problems of serious social concern in a way that has some retrospective aspects. *Blaisdell, supra,* 290 U.S. at 439. "The question is . . . whether the legislation is addressed to a legitimate end and the measures taken are reasonable and appropriate to that end." *Id.* at 438. Thus, the courts have balanced the competing interests by examining the challenged

statute from three perspectives: (1) whether the legislation deals with a matter of general social concern, (2) whether the statute is reasonable in scope, and (3) whether the precise degree of retrospective contract impairment effected by the enactment outweighs the public interest supporting the legislation. *See Allied Structural Steel Co.* v. *Spannus,* 438 U.S. 234, 240-44 (1978). We examine each of these questions in turn.

II. THE STATE PRICE PROTECTION ACTS DEAL WITH A SUBJECT OF SERIOUS, BROADLY BASED CONCERN TO THE PUBLIC

There can be no question but that the statutes at issue deal with a matter of widespread, indeed universal, public interest. The price of energy, including natural gas, affects all sectors of the economy and almost every individual citizen. Energy costs affect the price of every manufactured product. They are an important element in the cost of producing, processing and transporting the nation's farm goods. They have an immediate and dramatic impact on the transportation industries. They increase the cost of providing essential government services. And energy costs affect the utility bills and transportation costs of almost every individual American.

The price of natural gas has become a particularly serious problem in recent years. Between 1969 and 1977, prices increased by several hundred percent.[23] The impact of these escalations has been particularly severe at the household level. Some industrial and commercial users can switch with more or less ease to alternate fuels, but residential customers usually cannot. Many areas of the country are heavily dependent on natural gas for home heating. For example, approximately 90 percent of the homes in Oklahoma Natural's service area are heated by natural gas. Okla. Stip. ¶ 3(b). The effect of the mushrooming cost of energy has been so substantial that the

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23 *See* H.R. REP. No. 496, Part 4, 95th Cong., 1st Sess. 91 (1977); Staff of Subcomm. on Energy, Joint Economic Comm. of Congress, 95th Cong., 1st Sess., *The Economics of the Natural Gas Controversy* 18 (Comm. Print 1977).

government has found it necessary to provide large subsidies for the heating bills of low-income citizens.[24]

The Natural Gas Act of 1938 and the NGPA of 1978 compellingly demonstrate the firm and abiding public interest in ensuring that adequate supplies of natural gas will be produced and sold at fair prices. Moreover, this Court has recognized that the states also have a valid interest in regulating the intrastate aspects of natural gas production and sale. *See, e.g. Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*, 340 U.S. 179 (1950); *Palmer Oil Corp.* v. *Amerada Petroleum Corp.*, 343 U.S. 390 (1952).[25]

Indefinite price escalator clauses have specifically been held to be an appropriate subject of government regulation. In *Pure Oil Co.*, 25 F.P.C. 383 (1961), *aff'd*, 299 F.2d 370 (7th Cir. 1962), the FPC found that these contractual provisions were "contrary to the public interest" because they caused prices in many contracts to escalate upward, without any economic or other substantial justification, whenever higher prices are paid to another producer within a wide geographical area. *Id.* at 388-91. The FPC therefore promulgated a rule banning such clauses from any future contracts subject to its jurisdiction,[26] and this Court sustained the agency action in *FPC* v. *Texaco Inc.*, 377 U.S. 33 (1964). In 1965, the FPC extended this policy retrospectively to contracts executed prior to April 1961, by

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24 In 1981 Congress authorized the appropriation of $3 billion to subsidize the energy costs of low-income citizens. Home Energy Assistance Act of 1980, Pub. L. No. 96-223, 94 Stat. 288 (codified in scattered sections of 42 U.S.C.). A number of states have likewise acted to cushion the impact of dramatic increases in energy costs. *See, e.g.*, N.M. STAT. ANN. §§ 27-6-1 to -10 (1979) and N.Y. [SOC. SERV.] LAW § 370-aa (McKinney Supp. 1981).

25 Even prior to the NGPA and the Oklahoma and Kansas statutes, the State of New Mexico had declared an emergency in 1977 and imposed price controls on the wellhead price of natural gas sold to intrastate customers. 1977 N.M. Laws, ch. 73, §§ 2-13. This statute was modified and extended in 1979 and 1981. N.M. STAT. ANN. § 62-7-1 to -9.1 (Supp. 1981).

26 *Order No. 232*, 25 F.P.C. 379 (1961); *Order No. 232A*, 25 F.P.C. 609 (1961); *Order No. 242*, 27 F.P.C. 339 (1962).

prohibiting price escalators from causing rates to increase above the general area-wide rates then set by the agency. This Court sustained that action as well, finding that "[t]here is substantial evidence that in design and function [indefinite price escalator clauses] are 'incompatible with the public interest . . . .'" *Permian Basin Area Rate Cases,* 390 U.S. 747, 783 (1968).[27] Thus, it was well-established at the time of the State Price Protection Acts at issue, and appellant was on notice when it made its contracts, that indefinite price escalator provisions in natural gas contracts were a matter of serious concern and were subject to regulation.[28]

In areas such as this, which have traditionally been subject to extensive price-oriented regulation, Contract Clause objections to formally retroactive legislation have almost universally been rejected, because private agreements are thus made with knowledge that there may be "further legislation upon the same topic." *Veix* v. *Sixth Ward Building & Loan Association,*

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27 Appellant attempts to distinguish the foregoing FPC actions and court decisions by noting that the Contract Clause was not involved in those cases and by characterizing the FPC's prior restrictions as less objectionable than those imposed by the State Price Protection Acts. (Appt's Br. 40 n.55.) This misses the point. Regardless of whether the prior FPC actions and court decisions involved precisely the same legal issues as those presented here, they establish that indefinite price escalator clauses are a matter of legitimate public concern, so that state governments are acting within the proper scope of their police powers when they act to limit their effect.

28 Appellant's brief cites out of context *Kerr-McGee Corp.* v. *Northern Utilities, Inc.,* 673 F.2d 323 (10th Cir. 1982), for the proposition that Congress has expressly "struck the balance" in favor of indefinite price escalator clauses. (Appt's Br. 22, 29 n.41.) Appellant fails to note that the *Kerr-McGee* court ruled as it did only because (a) Wyoming had *not* enacted legislation pursuant to NGPA § 602 to restrict the effect of such clauses and (b) the Wyoming Supreme Court had expressly decided that such clauses were *not* contrary to Wyoming public policy. *Id.* at 327-28. In *Kerr-McGee,* the court recognized that the NGPA permitted the states to "restrict the operation of indefinite price escalator clauses if they choose to do so," and it cited the Kansas statute at issue here as an example of the exercise of a state's "right to alter the public policy expressed in the NGPA by enacting greater restrictions on the use of indefinite price escalation clauses." *Id.* at 327.

supra, 310 U.S. at 38. *See also Gelfert* v. *National City Bank,* 313 U.S. 221, 231-32 (1941). And so it is well-established that the state "has power to annul and supersede rates previously established by contract between utilities and their customers." *Midland Realty Co.* v. *Kansas City Power & Light Co.,* 300 U.S. 109, 113 (1937).

What is true on a utility's selling side is true on its buying side, particularly where the entity from whom the utility is buying its fuel has itself been subject to extensive price regulation. The present case not only involves an industry that has been pervasively regulated, but also involves particular aspects of that industry—long-term contracts with public utilities, wellhead pricing, and indefinite price escalator clauses—which have specifically been regulated prior to the contracts and the legislation at bar. *Contrast Allied Structural Steel, supra,* 438 U.S. at 247, 249.

The Oklahoma and Kansas statutes operate not in the private interest but in the public interest. The cost of fuel to gas and electric utilities is a major determinant of the rates that must be charged to consumers. In Oklahoma, increases and decreases in fuel costs are directly and almost immediately passed on to the utilities' customers.[29] In just the first two years of the statute (1979 and 1980), customers of Oklahoma Natural saved about $144 million as a result of the statute's

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29 OKLA. § 260.11(B), provides that if the price protection provisions of the statute are declared invalid or inoperative, and the gas purchase costs of any public utility or electric cooperative are thereby increased, the purchaser "shall be allowed to immediately include the amount of any such payment . . . in the calculations of its average cost of fuel . . . under any applicable fuel adjustment or purchased power adjustment clause . . . ." And even if the utility or cooperative has not previously been authorized to include a fuel adjustment or purchased power adjustment clause in its tariffs, the statute provides that the utility or cooperative "shall be authorized to charge its customers in an amount sufficient to reimburse it for all amounts so paid . . . ." Moreover, aside from the Price Protection Act itself, Oklahoma law provides for automatic pass-throughs of fuel price increases and decreases. OKLA. STAT. tit. 17, §§ 250-264 (1981). Oklahoma Natural *et al.* have approved fuel or purchased power adjustment clauses in their tariffs. Okla. Stip. ¶¶ 3(b)(ii), 22(b), 23(b).

regulation of indefinite price escalator clauses. Moreover, Oklahoma Natural prepared a forecast indicating that its customers and those of Public Service Co. and Oklahoma Gas & Electric Co. would save between $816,000,000 and $994,000,000 as a result of the Oklahoma statute during its six-year life. (*See* Okla. Litigation, Supp. Stip. No. 3, ¶ 9 and Exs. SS & TT, filed Oct. 22, 1980.)

It is clearly constitutional and in the public interest for the government to impose price controls in a situation such as this, where the effect on the public is substantial, where the price increases being sought are not based on increased operating costs, and where it is not claimed that the regulated prices are confiscatory.[30] And substantial deference is to be given to the judgment of the state legislatures when the courts are asked to decide whether statutes are within the proper scope of the state's police powers. *E.g., United States Trust Co., supra,* 431 U.S. at 22-23.

The judgment of Congress is not irrelevant to the question whether the State Price Protection Acts are a valid exercise of the states' power to regulate gas prices in the public interest. In the NGPA, Congress itself placed some limitations on indefinite price escalator clauses (*see* NGPA §§ 105(b)(3), 121(e) & 313 (reproduced in Appendix B)), and it clearly empowered the states to place additional restrictions on these clauses with respect to intrastate contracts for the sale of "old" gas. Given the prevalence of long-term gas supply contracts in the industry, to say that such a power could meaningfully be exercised by the states without some degree of effect on existing contracts would be to claim that Congress wanted the states to play "Hamlet" without Hamlet.

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30 *See, e.g., FPC* v. *Natural Gas Pipeline Co.,* 315 U.S. 575 (1942) (upholding constitutionality of Natural Gas Act of 1938); *FPC* v. *Hope Natural Gas Co.,* 320 U.S. 591 (1944) (upholding FPC rates for natural gas as just and reasonable). *See also Munn* v. *Illinois,* 94 U.S. 113 (1876) (upholding power of state to fix rates for public warehouses); *Nebbia* v. *New York,* 291 U.S. 502 (1934) (upholding power of state to establish minimum price for milk); *Bowles* v. *Willingham,* 321 U.S. 503 (1944) (upholding rent control provisions of the Emergency Price Control Act of 1942.)

Appellant asks this Court to strike down the State Price Protection Acts under the Contract Clause because, it says, the problem posed by indefinite price escalator clauses did not rise to the level of an "emergency." (Appt's Br. 28-30.) Appellant's rationale for this argument, that Congress had determined in the NGPA that price increases would be in the public interest, is erroneous: The NGPA *retained* price controls on "old" gas such as the gas involved in this case and provided for gradual price increases, while indefinite price escalator clauses would have produced dramatic escalations. Moreover, the Oklahoma legislature expressly found that an emergency *did* exist when it enacted the Oklahoma Natural Gas Price Protection Act,[31] and the Kansas legislation is addressed to the identical problem. The magnitude of the additional payments that otherwise would have been borne by consumers (pp. 18-19, *supra*) certainly demonstrates the adequacy of the emergency finding.

Appellant's argument also ignores the fact that the Contract Clause validity of retrospective adjustments in contracts does not depend on the existence of an "emergency." *E.g., Gelfert* v. *National City Bank, supra,* 313 U.S. at 235; *United States Trust Co., supra,* 431 U.S. at 22-23 n.19 (1977). However, where, as here, an emergency has been declared, that fact supports the legislation. *Blaisdell, supra,* 290 U.S. at 426.

III. THE STATE PRICE PROTECTION ACTS ARE REASONABLE AND APPROPRIATE IN SCOPE

As noted, the constitutionality of a state price regulatory statute claimed to impair the obligations of contracts depends, first, on whether the enactment is addressed to a legitimate end, and second, on whether the statute is "reasonable and appropriate" to that end. *Blaisdell, supra,* 290 U.S. at 438. This Court put it similarly in *United States Trust Co., supra,* 431 U.S. at 22: "Legislation adjusting the rights and responsibilities of contracting parties must be upon reasonable condi-

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31 Sen. Bill 49, 37th Okla. Legis., 1st Sess. § 15 (1979). This section of the Oklahoma Natural Gas Price Protection Act was not codified.

tions and of a character appropriate to the public purpose justifying its adoption." The Oklahoma and Kansas statutes meet this standard.

A. Appellant's Objections to the Scope and Approach of the State Price Protection Acts Are Without Merit

Appellant contends that the State Price Protection Acts do not legitimately deal with a substantial issue in the public interest because they regulate the prices of only a *portion* of the natural gas produced in the states, rather than comprehensively regulating *all* such prices. (*See* Appt's Br. at 10-11, 30-33.) This argument is wrong for several reasons.

Appellant first contends that the statutes are unduly narrow because they regulate only intrastate sales of natural gas, and not interstate sales. (*See* Appt's Br. 30-31.) But the States of Oklahoma and Kansas have no jurisdiction over the price of gas sold in interstate commerce. *Interstate Natural Gas Co.* v. *FPC*, 331 U.S. 682, 689 (1947). Indeed, Kansas once *did* attempt to regulate interstate aspects of this industry, and that effort was struck down by this Court. *Missouri ex rel. Barrett* v. *Kansas Natural Gas Co.*, 265 U.S. 298 (1924).

Appellant next finds fault with the fact that the State Price Protection Acts affect indefinite, but not fixed, escalator clauses. (Appt's Br. 30.) But there is a substantial difference in degree between the two types of contractual provisions. One is a blank check and the other is not. The contracts in this case contain fixed escalator provisions calling for a price increase of *two cents* per Mcf per year, which would have caused a 3.4% escalation in the contract price (from $1.79 to $1.85 per Mcf) in the three-year period from December 1978 to December 1981, whereas the indefinite price escalator clause would have produced a 66% escalation (from $1.79 to $2.97 per Mcf) during the same period. (*See* Appt's Br. 4 n.5 and Appendix.)[32]

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32 Similarly, there is a difference in degree between automatic, indefinite price escalations, which are regulated by the Oklahoma and Kansas statutes, and voluntary contract renegotiations, which are not. (*See* Appt's Br. 31.) Voluntary renegotiations of price are infrequent, and when they do

Appellant also complains that the state statutes do not apply to contracts executed after April 20, 1977 (Appt's Br. 30-31)—the date on which President Carter announced his proposed new energy policy. Appellant fails to note that this limitation on the Oklahoma and Kansas statutes was inserted for the benefit of gas *producers,* who might be thought to have had expectations of sharply higher prices after that date. The same date of April 20, 1977 is used as the base date for pricing purposes throughout the NGPA. *E.g.,* §§ 102(b) & 104(b).

Appellant mistakenly relies on *Allied Structural Steel, supra,* in support of its attack on the Oklahoma and Kansas statutes for narrowness. The fact that the states "appropriately tailored" their statutes to mesh with the NGPA *supports* the constitutionality of the enactments. 438 U.S. at 242. The "extremely narrow focus" (438 U.S. at 248) that concerned this Court there arose from the facts that that statute (i) benefited only a few people, (ii) applied to only a few employers, (iii) discriminated against companies that had been enlightened enough to establish pension plans, and (iv) had an extremely short duration. *Id.* at 247-50.[33] The alleged narrowness of the State Price Protection Acts is of a different character altogether. These statutes unquestionably will provide savings to the public at large, and appellant's argument is simply that even greater savings could have been provided if their coverage had been broader.

The constitutionality of state legislation does not depend on whether "it might have gone farther than it did, or [that] it

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occur it is because the parties have concluded that there is a substantial business reason to do so in the particular situation. Indefinite price escalator clauses, on the other hand, operate automatically and without economic justification in a multitude of contracts, based on circumstances which may not have been fully or legitimately anticipated by the parties.

33 This Court also based its decision in *Allied Structural Steel* on the facts that the Minnesota legislation attempted to avoid the preemption provisions in impending federal legislation; imposed sudden, unexpected regulation in a field never previously regulated by the state; and imposed a substantial liability on the plaintiff in potentially disabling amounts. *Id.* at 247-50. None of these factors is present here.

may not succeed in bringing about the result that it tends to produce." *Roschen* v. *Ward,* 279 U.S. 337, 339 (1929).[34] Thus, the fact that Oklahoma and Kansas did not absolutely prohibit *all* price increases for "old" gas, and the fact that some other statutes might have protected Oklahoma and Kansas consumers even more than the State Price Protection Acts did, does not detract from their validity.[35]

The thrust of appellant's argument—that the Oklahoma and Kansas statutes are defective because they *under*regulate intrastate natural gas prices—turns constitutional theory on its head. If it is true that the existing laws severely impair the right of gas producers to recoup the full value of their product, as appellant claims, then it is hard to see how an even broader deprivation of that value would be less objectionable to the producing interests or to the constitutional provision cited by them. It is ludicrous to argue that only a wholesale, and not a careful and precise, system of regulation is consistent with the Contract Clause. This is not a case like *Allied Structural Steel,* in which the statute's "extremely narrow focus" invidiously discriminated against or operated to the detriment of the plaintiff; here, the alleged underinclusiveness operates to the

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34 This Court has frequently reaffirmed this principle in a variety of contexts. *E.g., City of New Orleans* v. *Dukes,* 427 U.S. 297, 303 (1976) (rejecting equal protection challenge to a grandfather clause in a New Orleans ordinance regulating street vendors); *Williamson* v. *Lee Optical of Oklahoma, Inc.,* 348 U.S. 483, 489 (1955) (rejecting equal protection and due process attack on statute regulating prescription eyeglass sales, but not ready-wear eyeglass sales); *Railway Express Agency, Inc.* v. *New York,* 336 U.S. 106, 109-10 (1949) (rejecting due process and equal protection attack on traffic regulations that prohibited some, but not all, advertising on vehicles).

35 Likewise, appellant misses the point when it notes that the Oklahoma statute applies to a greater volume of gas than the Kansas statute does. (*See* Appt's Br. 12 n.20.) This is only because a greater percentage of Kansas' gas consumption comes from the interstate market. Section 104 of the NGPA already provides protection to Kansas consumers with respect to that interstate gas. The scope of the Oklahoma and Kansas statutes is identical; both are carefully tailored to fill the same regulatory gap in the NGPA that Congress left open to further state regulation.

benefit of, or at worst is neutral towards, natural gas producers.

Appellant is likewise wide of the constitutional mark when it suggests that the states should have allowed the escalator clauses to operate but required the public utilities to absorb the price increases without increasing their rates. (Appt's Br. 36-37.) That course of action, not the one actually chosen, would have posed serious constitutional difficulties. Regulated public utilities must be given a fair opportunity to earn a reasonable rate of return and therefore cannot be required to absorb hundreds of millions of dollars in cost increases without increasing their rates. *See, e.g., United Railways & Electric Co.* v. *West,* 280 U.S. 234, 249-52 (1930), *overruled on other grounds, FPC* v. *Hope Natural Gas Co., supra.*[36]

Appellant's alternative "solution"—*i.e.,* that the legislatures could have directed the utilities to impose the burden of the escalator-induced cost increases on industrial customers while sheltering individual consumers (Appt's Br. 37-38)—also misses the mark. First, appellant has not shown that it would be economically feasible to require one segment of energy users to

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36 The only authority cited by appellant for its extraordinary proposition is a statement in a treatise to the effect that state corporation commissions may require public utilities to absorb any costs that resulted from such things as "improvidence" or "abuse of managerial discretion," or expenses that are "inimical to the public interest." (Appt's Br. 31-32 n.44.) However, we understand appellant's position to be that its indefinite price escalator clauses are perfectly proper contractual provisions. Indeed, it states in its brief that it *insisted* on including such clauses in its contracts, because the contracts would have been unfair without them. If appellant's position is that it bullied the utilities into acts of improvidence in assenting to the clauses in question, that would not seem to make the clauses less subject to regulation in the public interest. (Appt's Br. 15, 21-22.) Moreover, the treatise cited by appellant makes clear (a) that it is not the function of rate-making authorities to second-guess the decisions of management and (b) that regulatory bodies must ordinarily base their decisions on the utility's actual operating expenses so long as they resulted from "an arm's length [transaction] and the price paid is within the realm of reason . . . ." 1 A. Priest, *Principles of Public Utility Regulation* 82 (1969). *See also id.* at 48, 50, 78, 81-82.

bear the burden of the massive price increases that would result from the price escalator clauses. Second, as appellant concedes, industrial users could switch to alternative fuels if prices to them were raised disproportionately (*see* Appt's Br. 37-38); this would save the utilities relatively little on the cost side and would result in even heavier burdens on residential customers in the long run.[37] Third, even if appellant's "solution" worked to any extent at the primary level, it probably would not ameliorate the inflationary effects of the price increases: Their full brunt would be imposed upon the economy of the State and, by one means or another, the cost would be passed on and the public would end up "paying the bill."

B. The State Price Protection Acts Do Not Constitute "Special Interest" Legislation

Appellant points to the fact that one public utility in Kansas purchased more than 40% of the intrastate natural gas covered by price escalator clauses, and it then leaps to the conclusion that the Kansas enactment constituted special-interest legislation. (Appt's Br. 9-10, 31-33.) Appellant's reasoning is faulty. In every state, the first purchase of most natural gas will be made by a small number of large public utilities, but this does not mean that those companies are the sole, or even primary, beneficiaries of reductions in the cost of fuel. It is frivolous to contend that utilities could incur millions of dollars in cost increases without affecting rates to consumers.

Appellant next argues that the Kansas statute should be struck down because it initially was approved in committee by a "narrow margin," because a few legislators had "misgivings" about the bill, and because at least one dissenter branded it as

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37 In the Oklahoma litigation, the parties stipulated that: "Facilities to serve industrial customers cost relatively little, and their absence would save Oklahoma Natural very little operational expense. However, the loss of the substantial revenue generated by these industrial customers would create a deficiency to be made up by the remaining customers." Okla. Stip. ¶ 31(e). *See also* H.R. Rep No. 496, Part 4, 95th Cong., 1st Sess. 98-99 (1977).

special-interest legislation. (Appt's Br. 10-12.)[38] These assertions are irrelevant, for a legislature is no more required to be unanimous than a court. Appellant also asserts that appellee was the "main proponent" of the Kansas legislation. (*Id.* at 9.) This simply boils down to the statement that appellee had an interest in, and therefore supported, the statute. Similar statements undoubtedly could be made about almost any other federal, state or local enactment.

IV. THE STATE PRICE PROTECTION ACTS DO NOT SUBSTANTIALLY IMPAIR APPELLANT'S CONTRACT RIGHTS

The Oklahoma and Kansas Price Protection Acts are moderate measures. They parallel the provisions of the NGPA in all respects, except for the operation of indefinite escalator clauses in old-gas contracts, and as to that, the state statutes accept an express invitation of Congress under NGPA § 602. Moreover, under the state statutes, producers are permitted to receive the *highest* price that would be lawful if the same gas were dedicated to interstate commerce.

Appellant asserts that when it executed its agreement with appellee, it relied heavily on the ability to reap the full "value" of its product. (Appt's Br. 21-27.) The term "value" is chimerical when applied to a regulated commodity such as natural gas, because natural gas sold in interstate commerce, even after the enactment of the NGPA, is sold at a broad range of prices under various extents of regulation. The theory of the NGPA, during a transitional period through December 31, 1984 (when the State Price Protection Acts also expire), is to reduce gas shortages by giving favorable regulatory price treatment to newly discovered and high-cost gas, while retaining more stringent price controls on "old" gas. This "mix" of prices

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38 The Kansas Natural Gas Price Protection Act passed the Kansas Senate by a vote of 36 to 3 and the Kansas House of Representatives by a vote of 92 to 31. In Oklahoma the vote was 32-14 in the Senate and 58-40 in the House.

keeps the overall price of gas to purchasers and consumers down to a fair and reasonable level. Thus, the price payable for the limited quantities of congressionally-favored natural gas cannot be said to represent "the" free-market "value" of the product as a whole. Congress was aware that the purchasers who are willing to pay high prices for the limited amount of the gas in the favored categories are averaging down their costs by purchasing gas in the other, cheaper categories under the NGPA. *See* H.R. REP. NO. 496, Part 4, 95th Cong., 1st Sess. 99 (1977).

It is quixotic to seek an answer to the question whether the value of appellant's natural gas is (i) the NGPA regulated price of "old" interstate natural gas, (ii) the marginal price that utilities and consumers of natural gas are willing to pay for "new" gas under a regime where they also have available to them quantities of less expensive "old" interstate gas, (iii) a "mix" or "average" of the various prices being paid, or (iv) some other price. There has certainly not been a free and unregulated wellhead price for natural gas in the United States for close to three decades, and that history has made the content of the term "value" for any type of natural gas an elusive, if not an empty one. *See Weymouth* v. *Colorado Interstate Gas Co.*, 367 F.2d 84, 88-90 (5th Cir. 1966). Thus, even if the extraordinary suggestion were accepted that price regulation by a state of a commodity vested with a public interest must not deprive its producer of its "full value," it could not be demonstrated that appellant was being deprived of such a price.

This Court's decisions in *Gelfert, supra,* and *City of El Paso* v. *Simmons, supra,* point the way to decision here. In *Gelfert,* a state statute restricted the effect of deficiency judgment clauses in mortgages by limiting the amount of deficiency judgments to the difference between the debt and the "fair and reasonable value" of the collateral.This Court rejected a Contract Clause attack on the statute, holding that parties to contracts have no constitutional right to receive more than their reasonable expectations. Likewise, in *City of El Paso* v. *Simmons,* this Court upheld a state statute that adjusted the

terms of Texas' long-term contracts for the sale of public lands. The Court noted that circumstances had changed over the years, and it observed that: "Laws which restrict a party to those gains reasonably to be expected from the contract are not subject to attack under the Contract Clause, notwithstanding that they technically alter an obligation of a contract." 379 U.S. at 515.

The purpose and effect of the Oklahoma and Kansas statutes is simply to prevent natural gas from being sold at windfall profits, to the detriment of the public at large. Appellant has no constitutional right to receive the windfall that would result from treating its "old" gas as § 102 "new" gas."

The State Price Protection Acts are only minimally retrospective. They inhibit only the prospective operation of contract provisions in place at the time of their enactment. They did not cause any "rollback" of prices currently being paid, let alone mandate any refund or rebate of payments already made by utilities to producers. In addition, the statutes are temporary and transitional in nature. They expire on December 31, 1984—simultaneously with the decontrol of many interstate prices—after giving the public a reasonable opportunity to adjust to the higher cost of natural gas.

Finally, even if appellant is correct when it states that it anticipated substantial future price increases when it executed its contract with appellee,[40] this would not render the law invalid, for the states "possess broad power to adopt general

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39 *Allied Structural Steel, supra,* upon which appellant relies so heavily, is not pertinent. Whereas that case involved a large, totally unexpected, potentially disabling *liability* that was retroactively imposed on a party to a contract, this is a case in which the state legislatures simply required gas producers to phase in their non-cost-justified *profit increases* so that the general public could absorb the impact gradually. *See also* p. 22, *supra.*

40 Despite appellant's assertions in its brief, it is highly questionable whether it truly expected back in 1975 and in earlier years that it would receive for its "old" gas the quantum increase in prices that Congress authorized several years later only for "new" gas. Such a gift of prophecy is rare. The *fixed* price escalator clauses in appellant's contracts called for a price increase of only $.02 per Mcf per year. (*See* Appt's Br. 4 n.5.)

regulatory measures without being concerned that private contracts will be impaired, *or even destroyed,* as a result." *United States Trust Co., supra,* 431 U.S. at 22 (emphasis added). This principle applies with particular force in the case of long-term contracts for an essential natural resource. It would be intolerable to permit private parties to avoid regulation by entering into a series of long-term arrangements. *See United States Trust Co., supra,* 431 U.S. at 22; *Hudson County Water Co.* v. *McCarter,* 209 U.S. 349, 357 (1908).

CONCLUSION

It is a flight of fancy to claim that the Oklahoma and Kansas statutes will make the Contract Clause a "dead letter" if they are sustained. (*See* Appt's Br. 20.) The danger lies in the opposite direction. If the states are not free to enact legislation that (a) deals with an industry which is heavily affected with the public interest and which has traditionally been regulated, (b) complements federal legislation on the same subject, (c) was enacted at the invitation of Congress, (d) governs wellhead natural gas prices, which have been regulated by the federal government for many years, (e) restricts indefinite price escalator clauses, which were found to be contrary to the public interest more than twenty years ago, and (f) prevents rapid, inflationary price increases while giving producers a fair and reasonable price, then a multitude of other state enactments regulating economic activities, and necessarily having some retrospective aspect, will be subject to serious challenge as well. Such a holding could well cause the federal judiciary to be involved in a multiplicity of cases, jeopardizing the ability of the individual states to address serious public issues.

In addition, if the State Price Protection Acts are struck down by this Court, the cause of federalism will receive a substantial blow. This Court would in effect be telling Congress that if it believed regulation of intrastate "old" natural gas prices was appropriate, it should have fully regulated the field itself, instead of expressly and consciously delegating to each gas producing state in § 602 of the NGPA the power to deal with this subject in its own way.

For the foregoing reasons, the judgment of the Kansas Supreme Court should be affirmed.

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APPENDIX A

EXCERPTS FROM STATE PRICE PROTECTION ACTS

Oklahoma Statute (OKLA. STAT. tit. 52, § 260.1 et seq. (1981))

§ 260.3 Application of act

Only natural gas purchase contracts entered into before April 20, 1977, providing for the sale, within this state, of natural gas produced in this state and not committed or dedicated to interstate commerce on November 8, 1978, shall be subject to the provisions of this act.

§ 260.4 Gas purchase contracts—Indefinite price escalator clause—Restrictions

Except to the extent provided in Sections 5 and 6, on or after December 1, 1978, the price allowed to be paid pursuant to federal legislation or any regulation by an agency implementing such legislation, or the price paid or to be paid for any sale of natural gas in the State of Oklahoma shall not be taken into account in applying any indefinite price escalator clause contained in any gas purchase contract subject to this act, to the

Kansas Statute (KAN. STAT. ANN., § 55-1401 et seq. (Supp. 1981))

55-1403. Applicability of act to natural gas purchase contracts.

Only natural gas purchase contracts entered into before April 20, 1977, providing for the sale, within this state, of natural gas produced in this state and not committed or dedicated to interstate commerce on November 8, 1978, shall be subject to the provisions of this act.

55-1404. Effect of indefinite price escalator clauses of certain natural gas purchase contracts on price of natural gas.

Except to the extent provided in K.S.A. 1979 Supp. 55-1405 and 55-1406, on or after December 1, 1978, the price allowed to be paid pursuant to federal legislation or any regulation by an agency implementing such legislation, or the price paid or to be paid for any sale of natural gas in the state of Kansas shall not be taken into account in applying any indefinite price escalator clause contained in any gas purchase contract subject

Oklahoma Statute (OKLA. STAT. tit. 52, § 260.1 et seq. (1981))

extent that such contract provides for the sale in the State of Oklahoma, of gas produced within this state which was not committed or dedicated to interstate commerce on November 8, 1978. This section shall not require a reduction of any price contained in any gas purchase contract subject to this act below the price actually paid prior to the date of enactment of this act.

§ 260.5 Indefinite price escalator clauses — Giving effect to — Calculation of maximum price — Exemptions

Notwithstanding the restriction on the operation of indefinite price escalator clauses imposed by Section 4 of this act, after the date of enactment of this act or March 1, 1979, whichever is earlier, such indefinite price escalator clauses in gas purchase contracts subject to this act may be given effect in accordance with their terms to the extent that the price payable under such contracts is not increased above the maximum price such gas would receive if it qualified under Section 109(b) of the Natural Gas Policy Act of 1978. The maximum price shall be calculated on a monthly basis. Nothing in this Sec-

Kansas Statute (KAN. STAT. ANN., § 55-1401 et seq. (Supp. 1981))

to this act, to the extent that such contract provides for the sale in the state of Kansas, of gas produced within this state which was not committed or dedicated to interstate commerce on November 8, 1978. This section shall not require a reduction of any price contained in any gas purchase contract subject to this act below the price actually paid prior to the date of enactment of this act.

55-1405. Same; limited effect of indefinite escalator clauses; price calculated monthly; exceptions.

Notwithstanding the restriction on the operation of indefinite price escalator clauses imposed by K.S.A. 1979 Supp. 55-1404, after March 1, 1979, such indefinite price escalator clauses in gas purchase contracts subject to this act may be given effect in accordance with their terms to the extent that the price payable under such contracts is not increased above the maximum price such gas would receive if it qualified under section 109(b) of the Natural Gas Policy Act of 1978. The maximum price shall be calculated on a monthly basis. Nothing in this section shall be construed to apply to gas pro-

Oklahoma Statute (OKLA. STAT. tit. 52, § 260.1 et seq. (1981))

tion 5 shall be construed to apply to gas produced from new wells, new reservoirs or stripper wells as defined by this act.

§ 260.6 New wells, reservoirs or stripper wells — Effecting indefinite price escalator clauses — Maximum price — Category determination

Notwithstanding the restriction on operation of indefinite price escalator clauses in gas purchase contracts imposed by Sections 4 and 5 of this act, after the date of enactment of this act or March 1, 1979, whichever is earlier, with respect to natural gas which is subject to this act, and which qualifies as gas produced from new wells, new reservoirs or stripper wells as defined in this act, such indefinite price escalator clauses may be given effect in accordance with their terms to the extent that the price payable under such contracts is not increased above the maximum price such gas would receive if it had been committed or dedicated to interstate commerce. The maximum price shall be calculated on a monthly basis. If the parties to the contract cannot agree as to the category of

Kansas Statute (KAN. STAT. ANN., § 55-1401 et seq. (Supp. 1981))

duced from new wells, new reservoirs or stripper wells as defined by this act.

55-1406. Same; effect of indefinite price escalator clauses on gas produced from new wells or reservoirs and stripper wells; price calculated monthly; category determinations.

Notwithstanding the restriction on operation of indefinite price escalator clauses in gas purchase contracts imposed by K.S.A. 1979 Supp. 55-1404 and 55-1405, after March 1, 1979, with respect to natural gas which is subject to this act, and which qualifies as gas produced from new wells, new reservoirs or stripper wells as defined in this act, such indefinite price escalator clauses may be given effect in accordance with their terms to the extent that the price payable under such contracts is not increased above the maximum price such gas would receive if it had been committed or dedicated to interstate commerce. The maximum price shall be calculated on a monthly basis. If the parties to the contract cannot agree as to the category of gas for which such gas qualifies

Oklahoma Statute (OKLA. STAT. tit. 52, § 260.1 et seq. (1981))

gas for which such gas qualifies under the terms of the Natural Gas Policy Act of 1978, then such category determination shall be made by the Commission.

§ 260.7 First sale of natural gas—Recovery of production, conservation and excise taxes

For purposes of this act, the price collected for the first sale of natural gas shall be permitted to exceed any maximum price established by this act, to the extent necessary to recover any production, conservation and excise taxes attributable to such natural gas.

§ 260.8 Voluntary renegotiation of gas purchase contract price provisions

Nothing contained in this act shall prevent or limit the voluntary renegotiation of price provisions contained in natural gas purchase contracts.

Kansas Statute (KAN. STAT. ANN., § 55-1401 et seq. (Supp. 1981))

under the terms of the natural gas policy act of 1978, then such category determination shall be made by the commission.

55-1407. Recovery of production and conservation fees and taxes.

For purposes of this act, the price collected for the first sale of natural gas shall be permitted to exceed any maximum price established by such sections of this act, to the extent necessary to recover any production and conservation fees and taxes attributable to such natural gas.

55-1408. Voluntary renegotiation of price provisions.

Nothing contained in this act shall prevent or limit the voluntary renegotiation of price provisions contained in natural gas purchase contracts.

Appendix B

PERTINENT EXCERPTS FROM NATURAL GAS POLICY ACT OF 1978 (15 U.S.C. § 3301 *et seq.* (Supp. IV 1980))

NGPA § 2 (15 U.S.C. § 3301). Definitions

. . .

(3) New well

The term "new well" means any well—

(A) the surface drilling of which began on or after February 19, 1977; or

(B) the depth of which was increased, by means of drilling on or after February 19, 1977, to a completion location which is located at least 1,000 feet below the depth of the deepest completion location of such well attained before February 19, 1977.

(4) Old well

The term "old well" means any well other than a new well.

. . .

(13) Existing contract

The term "existing contract" means any contract for the first sale of natural gas in effect on November 8, 1978.

. . .

NGPA § 102 (15 U.S.C. § 3312). Ceiling price for new natural gas and certain gas produced from the Outer Continental Shelf

(a) Application

The maximum lawful price computed under subsection (b) of this section shall apply to any first sale of natural gas delivered during any month in the case of—

(1) new natural gas; and

(2) natural gas produced from any old lease on the Outer Continental Shelf and qualifying under subsection (d) of this section for the new natural gas ceiling price.

(b) Maximum lawful price

The maximum lawful price under this section for any month shall be—

(1) $1.75 per million Btu's, in the case of April 1977; and

(2) in the case of any month thereafter, the maximum lawful price, per million Btu's, prescribed under this subsection for the preceding month multiplied by the monthly equivalent of a factor equal to the sum of—

(A) the annual inflation adjustment factor applicable for such month; plus

(B) (i) .035, in the case of any month beginning before April 20, 1981; or

(ii) .04 in the case of any month beginning after April 20, 1981.

(c) Definition of new natural gas

(1) General rule

For the purposes of this section, the term "new natural gas" means each of the following categories of natural gas:

(A) New OCS leases

Natural gas determined in accordance with section 3413 of this title to be produced from a new lease on the Outer Continental Shelf.

(B) New onshore wells

Natural gas determined in accordance with section 3413 of this title to be produced (other than from the Outer Continental Shelf) from—

(i) any new well which is 2.5 miles or more (determined in accordance with paragraph (2)) from the nearest marker well; or

(ii) any completion location, of any new well, which is located at a depth at least 1,000 feet below the deepest completion location of each marker well within 2.5 miles (determined in accordance with paragraph (2)) of such new well.

(C) New onshore reservoirs

(i) General rule

Except as provided in clauses (ii) and (iii), natural gas determined in accordance with section 3413 of this title to be produced (other than from the Outer Continental Shelf) from a reservoir from which natural gas was not produced in commercial quantities before April 20, 1977.

. . .

NGPA § 104 (15 U.S.C. § 3314). Ceiling price for sale of natural gas dedicated to interstate commerce

(a) Application

In the case of natural gas committed or dedicated to interstate commerce on November 8, 1978, and for which a just and reasonable rate under the Natural Gas Act [15 U.S.C. 717 et seq.] was in effect on such date for the first sale of such natural gas, the maximum lawful price computed under subsection (b) of this section shall apply to any first sale of such natural gas delivered during any month.

(b) Maximum lawful price

(1) General rule

The maximum lawful price under ths section for any month shall be the higher of—

(A)(i) the just and reasonable rate, per million Btu's, established by the Commission which was (or would have been) applicable to the first sale of such natural gas on April 20, 1977, in the case of April 1977; and

(ii) in the case of any month thereafter, the maximum lawful price, per million Btu's, prescribed under this subparagraph for the preceding month multiplied by the

monthly equivalent of the annual inflation adjustment factor applicable for such month, or

(B) any just and reasonable rate which was established by the Commission after April 27, 1977, and before November 9, 1978, and which is applicable to such natural gas.

(2) Ceiling prices may be increased if just and reasonable

The Commission may, by rule or order, prescribe a maximum lawful ceiling price, applicable to any first sale of any natural gas (or category thereof, as determined by the Commission) otherwise subject to the preceding provisions of this section, if such price is—

(A) higher than the maximum lawful price which would otherwise be applicable under such provisions; and

(B) just and reasonable within the meaning of the Natural Gas Act [15 U.S.C. 717 et seq.].

NGPA § 105 (15 U.S.C. § 3315). Ceiling price for sales under existing intrastate contracts

(a) Application

The maximum lawful price computed under subsection (b) of this section shall apply to any first sale of natural gas delivered during any month in the case of natural gas, sold under any existing contract or any successor to an existing contract, which was not committed or dedicated to interstate commerce on November 8, 1978.

(b) Maximum lawful price

(1) General rule

Subject to paragraphs (2) and (3), the maximum lawful price under this section shall be the lower of—

(A) the price under the terms of the existing contract, to which such natural gas was subject on November 9, 1978, as such contract was in effect on such date; or

(B) the maximum lawful price, per million Btu's, computed for such month under section 3312 of this title (relating to new natural gas).

(2) Contract price exceeding new gas ceiling price on November 9, 1978

In the case of any natural gas described in subsection (a) of this section for which the contract price applicable on November 9, 1978, exceeds the maximum lawful price, per million Btu's computed for such date under section 3312 of this title (relating to new natural gas), the maximum lawful price under this section shall be the higher of—

(A) the maximum lawful price, per million Btu's, computed for such month under section 3312 of this title; or

(B)(i) the contact[1] price on November 9, 1978, in the case of November, 1978; and

(ii) in the case of any month thereafter, the maximum lawful price, per million Btu's, prescribed under this subparagraph for the preceding month multiplied by the monthly equivalent of the annual inflation adjustment factor applicable for such month.

(3) Price increases resulting from indefinite price escalator clauses

(A) In general

Effective January 1985, and each month thereafter, in the case of any first sale of natural gas, which is sold at a price established under any indefinite price escalator clause of any existing contract or successor to an existing contract and for which the contract price on December 31, 1984, is higher than $1.00 per million Btu's, the maximum lawful price under this section for any such natural gas delivered during any month shall be the higher of—

(i) the maximum lawful price, per million Btu's, computed under paragraph (2)(B); or

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1 So in original. Probably should be "contract."

(ii)(I) in the case of January 1985, the maximum lawful price, per million Btu's, computed under section 3312 of this title (relating to new natural gas) for such month; and

(II) in the case of any month thereafter, the maximum lawful price, per million Btu's, prescribed under this clause for the immediately preceding month multiplied by the monthly equivalent of the sum of a factor equal to the annual inflation adjustment factor applicable for such month plus .03.

(B) Definition of indefinite price escalator clause

For purposes of this paragraph, the term "indefinite price escalator clause" includes any provision of any contract—

(i) which provides for the establishment or adjustment of the price for natural gas delivered under such contract by reference to other prices for natural gas, for crude oil, or for refined petroleum products; or

(ii) which allows for the establishment or adjustment of the price of natural gas delivered under such contract by negotiation between the parties.

(C) Contract modifications after May 3, 1978, to be disregarded

In the case of any natural gas which was subject to any contract on May 3, 1978, that contained an indefinite price escalator clause on such date, no amendment to or modification of the operation of such contract made after such date may have the effect of limiting or precluding the application of this paragraph on or after January 1, 1985, to prices allowed with respect to such natural gas.

(D) Exclusion

Subparagraph (A) shall not apply to any first sale of new natural gas (as defined in section 3312(c) of this title), stripper well natural gas (as defined in section 3318(b) of this title), high-cost natural gas (as defined in section 3317(c) of this title), natural gas produced from a new, onshore production well (as defined in section 3313(c) of this title) from a completion location located at a depth of more than 5,000 feet, and, beginning July 1, 1987, or, if later, the date of expiration of any price controls reimposed under section 3332 of this title,

natural gas produced under any new, onshore production well (as defined in section 3313(c) of this title) from a completion location located at a depth of 5,000 feet or less.

(c) Definition of contract price

For purposes of this section, the term "contract price", when used with respect to any specific date, means—

(1) the price paid, per million Btu's, under a contract for deliveries of natural gas occurring on such date; or

(2) if no deliveries of natural gas occurred under such contract on such date, the price, per million Btu's, that would have been paid had such deliveries occurred on such date.

NGPA § 107 (15 U.S.C. § 3317). Ceiling price for high-cost natural gas

(a) Wells completed below 15,000 feet

In the case of any first sale of high-cost natural gas produced from any well the surface drilling of which began on or after February 19, 1977, if such production is from any completion location which is located at a depth of more than 15,000 feet, the maximum lawful price under this section for such natural gas delivered during any month shall be the maximum lawful price, per million Btu's, computed for such month under section 3312 of this title (relating to new natural gas).

(b) Commission authority to prescribe higher incentive prices

The Commission may, by rule or order, prescribe a maximum lawful price, applicable to any first sale of any high-cost natural gas, which exceeds the otherwise applicable maximum lawful price to the extent that such special price is necessary to provide reasonable incentives for the production of such high-cost natural gas.

(c) Definition of high-cost natural gas

For purposes of this section, the term "high-cost natural gas" means natural gas determined in accordance with section 3413 of this title to be—

(1) produced from any well the surface drilling of which began on or after February 19, 1977, if such production is from a completion location which is located at a depth of more than 15,000 feet;

(2) produced from geopressured brine;

(3) occluded natural gas produced from coal seams;

(4) produced from Devonian shale; and

(5) produced under such other conditions as the Commission determines to present extraordinary risks or costs.

(d) Provisions for high-cost natural gas to be elective

If any credit, exemption, deduction, or comparable adjustment applicable to the computation of any Federal tax is specifically allowable with respect to any high-cost natural gas (or category thereof) under any provision of law enacted after November 9, 1978, the provisions of subsections (a) and (b) of this section and the provisions of part B of this subchapter shall not apply to such natural gas produced from any well unless an election to have such provisions apply (in lieu of such credit, exemption, deduction, or adjustment) with respect to such natural gas produced from such well is filed with the Commission on or before the later of—

(A) the 30th day after November 9, 1978, under which such credit, exemption, deduction, or adjustment is provided; or

(B) the date the surface drilling of such well began.

NGPA § 108 (15 U.S.C. § 3318). Ceiling price for stripper well natural gas

(a) General rule

In the case of any first sale of stripper well natural gas the maximum lawful price under this section for such natural gas delivered during any month shall be—

(1) $2.09 per million Btu's, in the case of May 1978; and

(2) in the case of any month thereafter, the maximum lawful price, per million Btu's, prescribed under this subsection for the preceding month multiplied by the monthly equivalent of a factor equal to the sum of—

(A) the annual inflation adjustment factor applicable for such month; plus

(B)(i) .035, in the case of any month beginning before April 20, 1981; or

(ii) .04, in the case of any month beginning after April 20, 1981.

(b) Definition of stripper well natural gas

(1) General rule

Except as provided in paragraph (2), the term "stripper well natural gas" means natural gas determined in accordance with section 3413 of this title to be nonassociated natural gas produced during any month from a well if—

(A) during the preceding 90-day production period, such well produced nonassociated natural gas at a rate which did not exceed an average of 60 Mcf per production day during such period; and

(B) during such period such well produced at its maximum efficient rate of flow, determined in accordance with recognized conservation practices designed to maximize the ultimate recovery of natural gas.

(2) Production in excess of 60 Mcf

The Commission shall, by rule, provide that, if nonassociated natural gas produced from a well which previously qualified as a stripper well under paragraph (1) exceeds an average of 60 Mcf per production day during any 90-day production period, such natural gas may continue to qualify as stripper well natural gas if the increase in nonassociated natural gas produced from such well was the result of the application of recognized enhanced recovery techniques.

(3) Definitions

For purposes of this subsection—

(A) Production day

The term "production day" means—

(i) any day during which natural gas is produced; and

(ii) any day during which natural gas is not produced if production during such day is prohibited by a requirement of State law or a conservation practice recognized or approved by the State agency having regulatory jurisdiction over the production of natural gas.

(B) 90-day production period

The term "90-day production period" means any period of 90 consecutive calendar days excluding any day during which natural gas is not produced for reasons other than voluntary action of any person with the right to control production of natural gas from such well.

(C) Nonassociated natural gas

The term "nonassociated natural gas" means natural gas which is not produced in association with crude oil.

NGPA § 109 (15 U.S.C. § 3319). Ceiling price for other categories of natural gas

(a) Application

The maximum lawful price computed under subsection (b) of this section shall apply to any first sale of any natural gas delivered during any month, in the case of any natural gas which is not covered by any maximum lawful price under any other section of this part, including—

(1) natural gas produced from any new well not otherwise qualifying for a higher maximum lawful price under this subchapter;

(2) natural gas committed or dedicated to interstate commerce on November 8, 1978, and for which a just and reasonable rate under the Natural Gas Act [15 U.S.C. 717 et seq.] was not in effect on such date for the first sale of such natural gas;

(3) natural gas which was not committed or dedicated to interstate commerce on November 8, 1978, and which was not subject to an existing contract on such day; and

(4) natural gas produced from the Prudhoe Bay Unit of Alaska and transported through the natural gas transportation system approved under the Alaska Natural Gas Transportation Act of 1976 [15 U.S.C. 719 et seq.].

(b) Maximum lawful price

(1) The maximum lawful price under this section for any month shall be—

(A) $1.45 per million Btu's, in the case of April 1977; and

(B) in the case of any month thereafter, the maximum lawful price, per million Btu's, prescribed under this paragraph for the preceding month multiplied by the monthly equivalent of the annual inflation adustment[1] factor applicable for such month.

(2) The Commission may, by rule or order, prescribe a maximum lawful ceiling price, applicable to any first sale of any natural gas (or category thereof, as determined by the Commission) otherwise subject to the preceding provisions of this section, if such price is—

(A) higher than the maximum lawful price which would otherwise be applicable under such provisions; and

(B) just and reasonable within the meaning of the Natural Gas Act [15 U.S.C. 717 et seq.].

NGPA § 121 (15 U.S.C. § 3331). Elimination of price controls for certain natural gas sales

(a) General rule

Subject to the reimposition of price controls as provided in section 3332 of this title, the provisions of part A of this

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1 So in original. Probably should be "adjustment."

subchapter respecting the maximum lawful price for the first sale of each of the following categories of natural gas shall, except as provided in subsections (d) and (e) of this section, cease to apply effective January 1, 1985:

(1) New natural gas

New natural gas (as defined in section 3312(c) of the title).

(2) New, onshore production wells

Natural gas produced from any new, onshore production well (as defined in section 3313(c) of this title), if such natural gas—

(A) was not committed or dedicated to interstate commerce on April 20, 1977; and

(B) is produced from a completion location which is located at a depth of more than 5,000 feet.

(3) Intrastate contracts in excess of $1.00

Natural gas sold under an existing contract, any successor to an existing contract, or any rollover contract, if—

(A) such natural gas was not committed or dedicated to interstate commerce on November 8, 1978; and

(B) the price paid for the last deliveries of such natural gas occurring on December 31, 1984, or, if no deliveries occurred on such date, the price would have been paid had deliveries occurred on such date is higher than $1.00 per million Btu's.

(b) High-cost natural gas

Effective beginning on the effective date of the incremental pricing rule required under section 3341 of this title, the provisions of part A of this subchapter respecting the maximum lawful price for the first sale of natural gas shall cease to apply to the first sale of high-cost natural gas which is described in section 3317(c)(1), (2), (3), or (4) of this title.

(c) Natural gas produced from 5,000 or less

Effective beginning July 1, 1987, or, if later, the date of expiration of any price controls reimposed under section 3332 of this title, the provisions of part A of this subchapter

respecting the maximum lawful price for any first sale of natural gas shall, except as provided in subsection (d) of this section, cease to apply to any first sale of natural gas produced from any new, onshore production well (as defined in section 3313(c) of this title), if such natural gas—

(1) was not committed or dedicated to interstate commerce on April 20, 1977; and

(2) is produced from a completion location which is located at a depth of 5,000 feet or less.

(d) Exclusion of certain Alaska natural gas

The provisions of subsections (a) and (c) of this section shall not apply to any natural gas produced from the Prudhoe Bay Unit of Alaska and transported through the natural gas transportation system approved under the Alaska Natural Gas Transportation Act of 1976 [15 U.S.C. 719 et seq.].

(e) Limitation on indefinite price escalators

Natural gas which is not subject to maximum lawful prices under part A of this subchapter solely by reason of subsection (a)(3) of this section and which is sold under any existing contract or successor to an existing contract at a price established under an indefinite price escalator clause (as defined in section 3315(b)(3)(B) of this title) shall be subject to the provisions of section 3315(b)(3) of this title.

NGPA § 313 (15 U.S.C. § 3373). Effect of certain natural gas prices on indefinite price escalator clauses

(a) High-cost natural gas

No price paid in any first sale of high-cost natural gas (as defined in section 3317(c) of this title) may be taken into account in applying any indefinite price escalator clause (as defined in section 3315(b)(3)(B) of this title) with respect to any first sale of any natural gas other than high-cost natural gas (as defined in section 3317(c) of this title).

(b) Other transactions

No price paid—

(1) in any sale authorized under section 3362(a) of this title [emergency purchase authority], or

(2) pursuant to any order issued under section 3363(b), (c), (d), or (g) of this title [emergency allocation authority],

may be taken into account in applying any indefinite price escalator clause (as defined in section 3315(b)(3)(B) of this title).

NGPA § 602 (15 U.S.C. § 3432). Effect on State laws

(a) Authority to prescribe lower maximum lawful prices

Nothing in this chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under subchapter I of this chapter.

(b) Common carriers

No person shall be subject to regulation as a common carrier under any provision of Federal or State law by reason of any transportation—

(1) pursuant to any order under section 3362(c) or section 3363(b), (c), (d), or (i) of this title; or

(2) authorized by the Commission under section 3371(a) of this title.

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Appendix C

NATURAL GAS CEILING PRICES (per MMBtu) [1]

"Old" Interstate Gas Prices	*Nov. 1978*	*Dec. 1978*	*Jan. 1979*	*Feb. 1979*	*March 1979*	*April 1979*	*May 1979*	*June 1979*	*July 1979*
Pre-1973 Wells									
Large Producer	$ .295	$ .332	$ .334	$ .336	$ .338	$ .340	$ .342	$ .344	$ .346
Small Producer	.384	.393	.395	.398	.401	.404	.407	.410	.413
1973-74 Wells									
Large Producer	.950	1.058	1.064	1.071	1.078	1.085	1.093	1.101	1.109
Small Producer	1.235	1.379	1.387	1.396	1.405	1.414	1.424	1.434	1.444
1975-February 1977 Wells	1.510	1.630	1.639	1.650	1.661	1.672	1.684	1.696	1.708
NGPA § 109 Prices	—	1.630	1.639	1.650	1.661	1.672	1.684	1.696	1.708
Range of Intrastate Prices Paid by Oklahoma Natural Under Contracts Subject to the Oklahoma Statute[2]	0.18–1.617[3]	0.18–1.645[3]	0.18–1.645[3]	0.18–1.645[3]	0.18–1.645[3]	0.18–1.645[3]	0.18–1.645[3]	0.18–1.696	0.18–1.708
NGPA § 102 "New" Gas Prices (wells drilled after February 19, 1977)	—	2.078	2.096	2.116	2.136	2.156	2.177	2.198	2.220

[1] Source: 18 C.F.R. § 271.101, Tables I & II, as supplemented by 47 Fed. Reg. 17981-85 (April 27, 1982).

[2] Table reflects prices actually paid to producers, net of state severance taxes.

[3] Prices paid by Oklahoma Natural prior to December 1978 were unregulated. These prices prevailed through May 1979, unaffected by §§ 102, 105 or 109 of the NGPA. However, after May 1979, Oklahoma Natural's prices under contracts limited by the Oklahoma statute have escalated to the NGPA § 109 prices except in the case of contracts that do not include indefinite escalator clauses.

Appendix C

NATURAL GAS CEILING PRICES (per MMBtu) [1]

	Aug. 1979	*Sept. 1979*	*Oct. 1979*	*Nov. 1979*	*Dec. 1979*	*Jan. 1980*	*Feb. 1980*	*Mar. 1980*	*April 1980*
"Old" Interstate Gas Prices									
Pre-1973 Wells									
Large Producer	$ .349	$ .352	$ .355	$ .357	$ .359	$ .361	$ .364	$ .367	$ .370
Small Producer	.416	.419	.422	.425	.428	.431	.434	.437	.440
1973-74 Wells									
Large Producer	1.118	1.127	1.136	1.144	1.152	1.160	1.168	1.176	1.184
Small Producer	1.456	1.468	1.480	1.490	1.500	1.510	1.521	1.532	1.543
1975-February 1977 Wells	1.722	1.736	1.750	1.762	1.774	1.786	1.799	1.812	1.825
NGPA § 109 Prices	1.722	1.736	1.750	1.762	1.774	1.786	1.799	1.812	1.825
Range of Intrastate Prices Paid by Oklahoma Natural Under Contracts Subject to the Oklahoma Statute[2]	0.18-1.722	0.18-1.736	0.18-1.750	0.18-1.762	0.18-1.774	0.18-1.786	0.18-1.799	0.18-1.812	0.18-1.825
NGPA § 102 "New" Gas Prices (wells drilled after February 19, 1977)	2.244	2.268	2.292	2.314	2.336	2.358	2.381	2.404	2.428

Appendix C

NATURAL GAS CEILING PRICES (per MMBtu) [1]

	May 1980	*June 1980*	*July 1980*	*Aug. 1980*	*Sept. 1980*	*Oct. 1980*	*Nov. 1980*	*Dec. 1980*	*Jan. 1981*
"Old" Interstate Gas Prices									
Pre-1973 Wells									
Large Producer	$ .373	$ .376	$ .379	$ .382	$ .385	$ .388	$ .391	$ .394	$ .397
Small Producer	.443	.446	.449	.453	.457	.461	.464	.467	.470
1973-74 Wells									
Large Producer	1.193	1.202	1.211	1.221	1.231	1.241	1.250	1.259	1.268
Small Producer	1.555	1.567	1.579	1.592	1.605	1.619	1.631	1.643	1.655
1975-February 1977 Wells	1.839	1.853	1.867	1.883	1.899	1.915	1.929	1.943	1.957
NGPA § 109 Prices	1.839	1.853	1.867	1.883	1.899	1.915	1.929	1.943	1.957
Range of Intrastate Prices Paid by Oklahoma Natural Under Contracts Subject to the Oklahoma Statute[2]	0.18–1.839	0.18–1.853	0.18–1.867	0.18–1.883	0.18–1.899	0.18–1.915	0.18–1.929	0.18–1.943	0.18–1.957
NGPA § 102 "New" Gas Prices (wells drilled after February 19, 1977)	2.453	2.478	2.504	2.532	2.560	2.588	2.614	2.640	2.667

Appendix C

NATURAL GAS CEILING PRICES (per MMBtu) [1]

	Feb. 1981	*March 1981*	*April 1981*	*May 1981*	*June 1981*	*July 1981*	*Aug. 1981*	*Sept. 1981*	*Oct. 1981*
"Old" Interstate Gas Prices									
Pre-1973 Wells									
Large Producer	$ .401	$ .405	$ .409	$ .412	$ .415	$ .418	$ .420	$ .422	$ .424
Small Producer	.474	.478	.482	.485	.488	.508	.511	.495	.497
1973-74 Wells									
Large Producer	1.279	1.291	1.303	1.311	1.319	1.327	1.334	1.341	1.348
Small Producer	1.670	1.685	1.700	1.711	1.722	1.733	1.742	1.751	1.760
1975-February 1977 Wells	1.975	1.993	2.011	2.024	2.037	2.050	2.060	2.070	2.080
NGPA § 109 Prices	1.975	1.993	2.011	2.024	2.037	2.050	2.060	2.070	2.080
Range of Intrastate Prices Paid by Oklahoma Natural Under Contracts Subject to the Oklahoma Statute[2]	0.18–1.975	0.18–1.993	0.18–2.011	0.18–2.024	0.18–2.037	0.18–2.050	0.19–2.060	0.19–2.070	0.19–2.080
NGPA § 102 "New" Gas Prices (wells drilled after February 19, 1977)	2.698	2.729	2.761	2.787	2.813	2.840	2.863	2.886	2.909

Appendix C

NATURAL GAS CEILING PRICES (per MMBtu) [1]

	Nov. 1981	*Dec. 1981*	*Jan. 1982*	*Feb. 1982*	*March 1982*	*April 1982*	*May 1982*	*June 1982*	*July 1982*
"Old" Interstate Gas Prices									
Pre-1973 Wells									
Large Producer	$ .427	$ .430	$ .433	$ .436	$ .439	$ .442	$ .443	$ .444	$ .445
Small Producer	.501	.505	.509	.513	.517	.521	.523	.525	.527
1973-74 Wells									
Large Producer	1.358	1.368	1.378	1.388	1.398	1.408	1.412	1.416	1.420
Small Producer	1.773	1.787	1.801	1.813	1.826	1.839	1.845	1.851	1.857
1975-February 1977 Wells	2.096	2.112	2.128	2.143	2.158	2.173	2.180	2.187	2.194
NGPA § 109 Prices	2.096	2.112	2.128	2.143	2.158	2.173	2.180	2.187	2.194
Range of Intrastate Prices Paid by Oklahoma Natural Under Contracts Subject to the Oklahoma Statute[2]	0.19–2.096	0.19–2.112	0.19–2.128	0.19–2.143	0.19–2.158	0.19–2.173	0.19–2.180	0.19–2.187	0.19–2.194
NGPA § 102 "New" Gas Prices (wells drilled after February 19, 1977)	2.940	2.971	3.003	3.033	3.063	3.093	3.112	3.132	3.152

Amicus Brief

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In the Supreme Court of the United States

OCTOBER TERM, 1982

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF OF AMICUS CURIAE

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No. 81-1370

In the
Supreme Court of the United States
OCTOBER TERM, 1982

ENERGY RESERVES GROUP, INC.,
Appellant,

v.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

On Appeal from the Supreme Court of Kansas

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

Comes now, the Corporation Commission of the State of Oklahoma and moves the Court for leave to file the attached brief *amicus curiae* to this case, pursuant to Supreme Court Rule 36.4. As this brief is being filed on behalf of the Oklahoma Commission by and with the Attorney General of the State of Oklahoma pursuant to Supreme Court Rule 36.4, consent of the attorneys for Appellant and Appellee is not required.

The Oklahoma Corporation Commission regulates natural gas from the preliminary stages before drilling (52 O.S. 1981, §87.1) to the method and rates of home and industrial delivery (17 O.S. 1981, §151 *et seq.*). The Commission has the responsibility to make category determinations under the federal Natural Gas Policy Act of 1978

(NGPA) (15 U.S.C. §3301 *et seq.*) and administers and enforces the Oklahoma Natural Gas Price Protection Act (52 O.S. 1981, §260.1 *et seq.*) (Oklahoma Act).

The Kansas Natural Gas Price Protection Act (K.S.A. §55-1401 *et seq.*) (Kansas Act) was patterned after and is substantially identical to, the Oklahoma Act. The determination of the constitutionality of the Kansas Act in this case will have a substantial impact on the determination of the validity of the Oklahoma Act. The members of the Corporation Commission are the named defendants in an action questioning the constitutionality of the Oklahoma Act in the United States District Court for the Western District of Oklahoma (*Energy Consumers and Producers Association, et al.* v. *Baker, et al*, W.D.Ok., Civ. Nos. 79-320-D and 79-823-D). Briefing is complete in the Oklahoma case, but no decision on the merits has been rendered.

Natural gas is a very significant source of energy in Oklahoma. This significance led to an early sensitivity on the part of Oklahoma state legislators to the impact of the NGPA on Oklahoma gas prices.

Since gas prices are so significant in Oklahoma, the impact of a declaration that the Kansas Act is constitutional, or otherwise, will have immediate impact in Oklahoma. Early estimates indicated as much as $994,345,520.00 would be saved by Oklahoma utility ratepayers by operation of the Oklahoma Act through 1985 (Exhibit "55", *Energy Consumers and Producers Ass'n* v. *Baker, supra.* Stipulation 3). Conversely, that is the amount of potential liability the ratepayers would have if the Oklahoma Act were declared unconstitutional, for that Act requires

the pass-through of unpaid prices to the ratepayer (52 O.S. 1981, §260.12).

All of the foregoing makes the decision in this case very important to the Oklahoma public and the Oklahoma Commission. The Oklahoma Commission's familiarity with the origin and purpose of the Oklahoma Act may provide some additional insight to the Court in disposing of the pending appeal.

Respectfully submitted,

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BRIEF AMICUS CURIAE OF THE OKLAHOMA CORPORATION COMMISSION, BY AND WITH THE ATTORNEY GENERAL OF OKLAHOMA

STATEMENT OF INTEREST OF AMICUS CURIAE

The interest of the Oklahoma Corporation Commission, appearing by and through the Attorney General of Oklahoma, is set forth in the accompanying Motion for Leave to File Brief *Amicus Curiae*.

STATEMENT OF FACTS

In order to understand the Kansas Natural Gas Price Protection Act (Kansas Act) (K.S.A. §§55-1401 - 55-1415, Supp. 1981) and the Oklahoma Natural Gas Price Protection Act (Oklahoma Act) (52 O.S. 1981, §§260.1-260.13), this Court needs to know some of the basic history of natural gas regulation. It will be useful to have a brief chron-

ological overview of the conditions which led to the enactment of the Natural Gas Policy Act (NGPA) (15 U.S.C. §3301 *et seq.*). The legislative history of the NGPA and the Oklahoma Act can provide insight on the questions of constitutional law presented in this case. Some of the events occurring after the passage of the Oklahoma Act also have significance for this case.

1. Natural Gas Regulation Before the NGPA

Shortly after Oklahoma became a State in 1907, the Oklahoma Corporation Commission was given wide powers to regulate gas and gas pipelines. This law, passed in 1913, also gave the Commission the power to establish prices in cases of dispute, and minimum prices to prevent waste, 52 O.S. 1981, §§233 - 234.

The federal government became involved in the pricing of natural gas with the passage of the Natural Gas Act (NGA) in 1938 (15 U.S.C. §§717 - 717w). The federal law established utility-type proceedings for interstate pipelines, including certificates of convenience and necessity. The Federal Power Commission (FPC) administered the NGA, and in 1939 required pipelines to show long-term contracts in order to obtain a certificate.[1] The first price escalation provisions in gas contracts have been attributed to this government action.[2]

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[1] *In the Matter of Kansas Pipeline and Gas Co. and North Dakota Consumers Gas Co.*, 2 FPC 29 (1939).

[2] 4 Williams & Meyers, Oil and Gas Law, §726 (1981) as explained in Williams and Meyers, there are several kinds of escalation clauses. Basically, there are definite escalator clauses (which increase the contract price by a fixed amount), and indefinite escalator clauses (which increase the contract price based on some factor outside the contract. Wil-

In 1950, this Court rejected challenges to the Oklahoma Corporation Commission's exercise of price control over intrastate prices, *Cities Service Gas Co.* v. *Peerless Oil and Gas Co.*, 340 U.S. 179 (1950). Four years later, this Court issued the landmark *Phillips Petroleum* v. *Wisconsin* decision, 347 U.S. 672 (1954), which held that the FPC had jurisdiction over the wellhead price of natural gas sold in interstate commerce.

The FPC tried to establish these prices by company-by-company determinations, but soon had an enormous backlog.[3] In 1960, the FPC abandoned that approach, and attempted to produce an "area rate" for producing regions.[4] In 1961, indefinite price escalator clauses in interstate contracts were found to be contrary to public policy.[5] This Court sustained the FPC in that determination in *FPC* v. *Texaco, Inc.*, 377 U.S. 33 (1964). In 1965, the first "area rate" case was completed for the Permian Basin, and this Court sustained the FPC's use of area rate proceedings, and found that there was substantial evidence "that in design and function [indefinite price escalator clauses] are incompatible with the public interest", *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968).

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[2] (Continued)
liams and Meyers explain and give examples of the several types of indefinite price escalator clauses, including most favored-nations clauses, third-party most-favored-nation clauses, and spiral escalation clauses.

[3] See J. Landis, Report on Regulatory Agencies to the President-Elect, reprinted in Staff of Senate Comm. on the Judiciary, Report on Regulatory Agencies to the President-Elect, 86th Cong., 2nd Sess., at 55 (1960).

[4] Permian Basin Area Rate Proceeding, 34 FPC 159 (1965).

[5] Pure Oil Co., 25 FPC 383 (1961).

The long lag between the initiation and conclusion of FPC hearings establishing rates led to substantially lower prices in the federally-regulated interstate market than in the unregulated intrastate market. This caused severe shortages on the interstate market. Finally, in the Winter of 1976-1977, there were 75 gas-shortage related deaths and two million workers laid off.[6] This natural gas crisis led President Carter on April 20, 1977, to call for permanent price controls on all natural gas production, as part of an energy program he called the "moral equivalent of war".[7] In 1977, the New Mexico Legislature responded with the New Mexico Natural Gas Pricing Act,[8] which restricted the operation of indefinite price escalator clauses in that state.

2. The Creation of the Natural Gas Policy Act

After President Carter's speech, the President's plan was introduced in both the House of Representatives[9] and the Senate.[10] The House approved the President's plan on August 5, 1977.[11] The Senate, however, adopted a substitute plan put forth by Senators Pearson and Bentson on October 4, 1977.[12] The House bill extended permanent

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[6] Wall Street Journal, Feb. 1, 1977, page 1, col. 3.

[7] Reprinted at 123 Cong. Rec. H3328 (daily ed., April 20, 1977).

[8] N. Mex. Stat. Ann., §67-7-2 to -9 (1977).

[9] H. R. 8444, 95th Cong., 1st Sess. (1977).

[10] S. 1469, 95th Cong., 1st Sess. (1977).

[11] 123 Cong. Rec. H8826-27 (daily ed. Aug. 5, 1977) (Roll No. 513). The vote was 244 to 177.

[12] 123 Cong. Rec. S16323-25 (daily ed. Oct. 4, 1977). The vote was 50-46.

price controls to the intrastate market. The Senate plan set interim price ceilings pending phased-in deregulation. The Senate bill would have *increased* producer revenues by sixty to seventy-five billion dollars during the period from 1977 to 1985. The House Bill would have *reduced* producer revenues by at least fourteen billion dollars during the same period.[13]

With the two bodies divided so widely, both bills went to a Joint Conference Committee. On May 23, 1978, the House Conferees narrowly agreed to an agreement in principle, after adopting modification proposed by Rep. Eckhardt of Texas explicitly protecting the state's rights to control indefinite price escalator clauses.[14] The agreement explicitly provided:

> "C. State authority to limit or prohibit the operation of any indefinite price escalator clause or limit their effect, *e.g.*, through a state-imposed ceiling price (see Part XVI.A.) would not be preempted, *i.e.*, State may prescribe more stringent limitations on the operation of such clauses than those prescribed herein."[15]

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[13] Proposed Joint Explanatory Statement of the Committee in Conference on H.R. 5289, "Economic Analysis of Conference Agreement" (July 31, 1978). See Ligon, "Problems of Contractual Authorization to Collect NGPA Wellhead Prices", 57 Tex. L. Rev. 551, 552 (1979), hereinafter referred to as "Ligon, 'Problems' ". This article is the only apparent source for some of the inside history of the NGPA.

[14] Ligon, "Problems", *supra* note 13, at 553, fn. 18. This was specifically to protect the New Mexico statute and any similar statutes, Natural Gas Policy Act Information Services, ¶602:901 (1979).

[15] Staffs of House Comm. on Interstate and Foreign Commerce and Senate Comm. on Energy and Natural Resources, 95th Cong., 2d Sess., Natural Gas Pricing Agreement Adopted by the Conferees on H.R. 5289 (Comm. Print No. 95-55, 1978) p. 18.

The House proposal with the Eckhardt amendment was approved by the Senate Conferees on May 24, 1978.[16]

The final version of the bill with major modifications, was released by the Conference on August 16, 1978, with an important Conference Committee explanation attached.[17] With regard to states' power to set prices, Section 602 of the bill provided:

> "Nothing in this Act shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under title I of this Act."

In the Conference Committee Report, the Conferees explained the meaning of this provision:

> "The conference agreement provides that nothing in this Act shall affect the authority of any State to establish or enforce any maximum lawful price for sales of gas in intrastate commerce which does not exceed the applicable maximum lawful price, if any, under Title I of this Act. This authority extends to the operation of any indefinite price escalator clause. The Congress enacts this provision with a recognition that it is ceding its authority under the commerce clause of the Constitution to regulate prices for such production to affected States."[18]

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[16] Ligon, "Problems", *supra* note 13, at 553, fn. 18. The vote was 10 to 7.

[17] Joint Explanatory Statement of the Comm. on Conference, H.R. Rep. No. 1752, 95th Cong., 2d Sess.; S. Rep. No. 1126, 95th Cong., 2d Sess.; *reprinted* in [1978] U.S. Code Cong. & Ad. News 9041. Both reports are identical.

[18] Senate and House Reports at 124-25 (1978).

Similarly, the Conferees explained Section 105 of the NGPA by noting the Congress had specifically limited the operation of indefinite price escalators:

> "The conference agreement specifically prohibits prices paid in any sale of high-cost natural gas from triggering the operation of any indefinite price escalator clauses. The conference agreement also cedes the Federal Government's authority to further limit the operation of indefinite price escalator clauses to State governments wishing to do so. The Congress, by adoption of this section, recognizes the right of States to prescribe more stringent limitations on the operation of such clauses than those prescribed herein."[19]

On September 27, 1978, the Senate passed the NGPA by a vote of 57-42.[20] The Carter Administration decided to back the bill, and on October 13, 1978, the House agreed by one vote on a crucial procedural motion to consider the National Energy Act as a package.[21] On the last day of the 95th Congress, October 15, 1978, the House approved the entire energy package.[22] President Carter signed the energy acts, including the NGPA, on November 9, 1978.[23]

The provisions of the NGPA are explained at length in the other briefs in this case, so Oklahoma's discussion can be very brief. "Old" intrastate gas was placed under federal regulation, and had a ceiling set by 15 U.S.C. §3315

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[19] *Id.*, at 83 (1978).

[20] 124 Cong. Rec. S16265 (daily ed. Sept. 27, 1978).

[21] 124 Cong. Rec. H12819 (daily ed. Oct. 13, 1978).

[22] 124 Cong. Rec. H13426-27 (daily ed. Oct. 15, 1978). The vote was 231 to 168.

[23] 124 Cong. Rec. H13704 (daily ed. Nov. 15, 1978).

at the lower of the contract price or the "New" gas price ceiling set by Section 102 (15 U.S.C. §3312). Depending on the exact language of the contract, indefinite price escalator clauses would raise the contract price to the highest permitted price, the 102 price. The 102 price goes up each month by operation of an "inflation adjustment factor", plus a percentage bonus of 3.5 percent (before April 20, 1981) or 4 percent (after April 20, 1981).

The 109 price is also significant for this case because that ceiling is the one picked by the Oklahoma and Kansas Legislatures. The 109 price is a miscellaneous "other" gas provision which took the highest price of "old" interstate gas and added the inflation adjustment factor each month (15 U.S.C. §3319). Each of these prices becomes significant in the discussion to follow.

3. The Creation of the Oklahoma Natural Gas Price Protection Act

The Brief of the Energy Reserves Group goes into the legislative history of the Kansas Act in great detail, in a vain attempt to make this case appear similar to *Allied Structural Steel* v. *Spannaus*, 438 U.S. 234 (1978). The Oklahoma experience in formulating the pattern of the Kansas Act thus becomes important. Even if the attempt to make the Kansas facts fit the *Allied Steel* mold were successful, a consideration of the *entire* history of the Oklahoma Act destroys the theory that this case is at all similar to *Allied Steel*.

On May 24, 1978, the United States Conferees agreed to the House agreement in principle, including the explicit recognition of state power over indefinite price escalator

clauses offered by Representative Eckhardt of Texas.[24] On May 30, 1978,[25] Oklahoma State Senate President Pro Tempore Gene Howard[26] called a press conference to urge the Governor to call a special session of the Oklahoma Legislature. The purpose of the special session was to limit the effect of the NGPA on Oklahoma escalator clauses.

On September 15, 1978, about a month after the release of the Joint Conference Committee report in Congress, Senator Howard presented a proposal to the Executive Committee of the State Legislative Council,[27] once again calling for action on the problem of indefinite price escalator clauses. The Executive Committee took no action.

On October 4, 1978, Governor David Boren created a 15-member "blue ribbon" committee composed of his energy advisers, and representatives from the gas industry, the utilities, and academia. The task of the committee was to study the NGPA, assess its effects on Oklahoma, recom-

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[24] See fn. 16 and accompanying text.

[25] This date and other dates in 1978 are derived both from contemporary news accounts in the *Oklahoma Legislative Reporter*, a privately-published newsletter of limited distribution which comprehensively covers Oklahoma governmental affairs, and the memory of the author of this brief, who worked for the Oklahoma Legislature in 1978 and 1979, as a legislative draftsman and was personally involved in the drafting of Senate Bill 49 and related bills.

[26] The President Pro Tempore is the highest officer in the Oklahoma State Senate. Unlike other states and the United States Senate, the President Pro Tem actually is the most powerful senate officer in Oklahoma.

[27] The Executive Committee of the State Legislative Council was composed of the "leadership" of both houses who met during the interim between sessions of the Legislature to study and discuss legislative action for the upcoming legislature.

mend any actions that Oklahoma could take, and advise the Governor on the need for a special session.

On November 15, 1978, the Special Committee voted not to recommend a special session, since the regular legislative session was so close. On November 29, Speaker of the House Dan Draper joined Senator Howard in urging a special session. On December 6, 1978, Governor Boren announced he would not call a special session and transmitted the work of the special committee to incoming Governor George Nigh.

The Oklahoma Legislature convened on January 2, 1979. Senate Bill No. 49 by Howard and Draper was introduced, limiting escalator clauses to the 109 price.[28] House Bill 1107 by Representative Wiseman and Senator Cate was introduced in the House the next day.[29] The Wiseman-Cate bill imposed a one-year moratorum on the operation of escalator clauses, with limited increases after that time. On January 9, the relevant House and Senate Committees held separate hearings on their respective bills. Several witnesses appeared before both committees, both in favor of and opposing the legislation. On January 15, House Bill 1206 by Hobson and 1212 by Wiseman were introduced.[30] Both bills would have vested the Oklahoma Corporation Commission with the task of making category determinations under the NGPA. Both bills were strongly favored by producers, who could not obtain higher prices for their wells until their category was established.

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[28] Oklahoma Senate Journal, January 3, 1979.

[29] Oklahoma House Journal, January 4, 1979.

[30] *Id.*, January 15, 1979.

On February 6, the Oklahoma Senate passed S.B. 49 by a vote of 32 to 14, after several floor amendments.[31] On March 8, SB 49 was adopted by the House of Representatives with a vote of 58 to 40 on the bill and a vote of 68 to 31 on the separate declaration of an emergency.[32] The Senate concurred in House amendments on March 13, 1979 by a vote of 26 to 18 on the bill, and a vote of 32 to 11 on the emergency.[33] Governor George Nigh signed both HB 1206 and SB 49 into law on March 19, 1979.

The Oklahoma Act closely tracked the NGPA as passed by Congress. The definitions were lifted verbatim from the NGPA. New gas was allowed to go to the 102 price, and "stripper" gas was allowed to go to the 108 price for the same type of wells (52 O.S. 1981, §260.5). The only limits in the bill were placed on indefinite price escalator clauses in contracts for old intrastate gas (52 O.S. 1981, §260.3). Those clauses were restricted in operation to take the price to the 109 price (52 O.S. 1981, §260.5). Parties were given the ability to renegotiate voluntarily the pricing provisions of their contracts (52 O.S. 1981, §260.8). The Oklahoma Corporation Commission was required to monitor the effect of the Act and report annually to the Legislature until the Act expired on December 31, 1984 (52 O.S. 1981, §260.13).

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[31] Senate Journal, February 6, 1979.

[32] House Journal, March 8, 1979. The separate vote on the emergency is required by Oklahoma Constitution, Article V, §58, which requires a two-thirds majority of each house to make a bill effective immediately upon approval by the Governor.

[33] Senate Journal, March 13, 1979.

4. Events After the Passage of the Oklahoma Natural Gas Price Protection Act

Natural gas producers wasted no time in challenging the Oklahoma Natural Gas Price Protection Act (S.B. 49). One day after it was signed into law, suit for declaratory judgment was brought in the United States District Court for the Western District of Oklahoma, with the style *Energy Consumers and Producers Association* v. *Baker,* Civ. 79-320-D. A week later a similar suit was brought in the United States District Court for the Northern District of Oklahoma, *Oklahoma Independent Petroleum Association* v. *Baker,* Civ. 79-C-174-C (March 27, 1979). The cases were later consolidated in the Western District and are still pending.

On February 6, 1979, S.B. 252 had been introduced in the Kansas Senate (coincidentally the same day S.B. 49 was passed by the Oklahoma Senate). On April 25, 1979, the subject of this litigation, H.B. 2680 was introduced in the Kansas House. On May 14, 1979, the Kansas Act was approved by the Kansas Legislature.

On November 24, 1980, the validity of the Kansas Act was upheld in *Edmiston* v. *State Corporation Commission,* No. 79-1335 (D. Kan. Nov. 24, 1980) *modified* (D. Kan. Jan. 13, 1981), *appeal docketed* No. 71-1197 (10th Cir. Feb. 23, 1981). On July 17, 1981 the Kansas Supreme Court upheld the validity of *Energy Reserves Group, Inc.* v. *Kansas Power and Light Co.,* 230 Kan. 176, 630 P.2d 1142 (1981).

SUMMARY OF ARGUMENT

The question in this case involves the validity of the Kansas Natural Gas Price Protection Act in light of a constitutional challenge based on the Contract Clause, Article I, Section 10, United States Constitution. Previous decisions of this Court have listed several factors useful in determining whether a given legislative action is valid under the Clause. First, the Court must determine whether a substantial impairment of the contractual relationship occurred at all, *Allied Structural Steel Co.* v. *Spannaus*, 438 U.S. 234, 244 (1978), with the severity of the impairment measuring the "height of the hurdle the state legislature must clear", *Id.* at 245. If the legislation is in response to an unforeseen development which alters the manner in which the original contract provisions impact upon the public interest, that is a factor in favor of the legislation's validity, *Home Building and Loan Association* v. *Blaisdell*, 290 U.S. 398, 426 (1934); *El Paso* v. *Simmons*, 379 U.S. 497, 515 (1965). The act must address a legitimate public end, not the mere advantage of particular individuals, *Blaisdell*, 290 U.S. at 445; *Allied Steel*, 438 U.S. at 250. A factor in assessing both whether the contract was impaired and the end was legitimate is the existence of state regulation of the general subject-matter at the time the contract was made, *Veix* v. *Sixth Ward Building and Loan Association*, 319 U.S. 32, 38 (1940); *Allied Structural Steel*, 438 U.S. at 250. The legislation must have reasonable conditions and be of a character appropriate to the public purpose, *United States Trust Co.* v. *New Jersey*, 431 U.S. 1, 22-23 (1977). Finally, it is a factor in the act's favor if it is of temporary duration, *Blaisdell*, 290 U.S. at 447; *Allied Structural Steel*, 438

U.S. at 250. Utilizing these tests in this case leads to the conclusion that both the Oklahoma and Kansas Acts are valid exercises of the states' police powers and should be sustained by this Court.

(a) The contract provisions in this case were not severely impaired by the Kansas Act. The Constitution protects the expectation and reliance interests of the parties to a contract. In this case, the contracts specifically contemplate state action and the parties expressly incorporated any changes in state law into their contract.

(b) This Court traditionally grants great deference to the legislative judgment in passing laws regulating the economic affairs of a state. This deference should be extended to the legislatures of New Mexico, Oklahoma, and Kansas, who fought over and passed price protection acts for the benefit of their citizens.

(c) The Oklahoma and Kansas Acts were in response to an unforeseen and unforeseeable revolution in the matter in which the federal government treated intrastate natural gas prices. The NGPA was a radical renewal of federal policy, which altered the effects of private contracts on the public interest. Oklahoma and Kansas met this unforeseen political action of Congress with political action of their own, to minimize the effects of the NGPA revolution.

(d) The Oklahoma and Kansas Acts were enacted to deal with broad, generalized economic problems. This case has little in common with *Allied Structural Steel*, 438 U.S. 234 (1978), in which only narrow, limited interests were served. Both states have a substantial interest in natural

gas and the impact of the price of natural gas. The Oklahoma and Kansas Legislatures also had a legitimate purpose in preventing an unearned and unjustified windfall to producers from the increase of prices for old natural gas. Both of these purposes were recognized as legitimate by the United States Congress when it passed the NGPA, and expressly provided that states could regulate the price of intrastate gas.

(e) At the time of the contract, the area of natural gas regulation was already one in which Oklahoma and Kansas were active. Persons in the industry know they are subject to further state regulation. The parties in this case clearly reflected in their contracts the fact that they knew they were subject to further state regulation. This demonstrates both the amount of impairment of the contracts is low, and that this area of regulation is a legitimate one for state action.

(f) The Acts in question have reasonable conditions and are of a character appropriate to their public purpose. The Oklahoma and Kansas legislatures are the primary judges of the reasonableness of their actions. Actions restraining the operation of indefinite price escalator clauses to a gradual increase is a reasonable response to the goals of protecting ratepayers and preventing windfalls. Such clauses have not been looked upon with favor by either regulators or courts; and it is in the public interest to modify them in a reasonable manner.

(g) Finally, both the Oklahoma and Kansas Acts are temporary in nature, expiring December 31, 1984. That is the scheduled expiration date of the unforeseen event they

were designed to meet, *i.e.*, the NGPA. This temporary operation means that producers can look forward to a fixed day that they will be free of *state* price regulation.

Reviewing all of the factors this Court has utilized in the past, it is clear that the Kansas Act is not a law impairing the obligation of contracts as prohibited by the Contract Clause of the United States Constitution. This Court should affirm the decision of the Kansas Supreme Court.

ARGUMENT

I. THE KANSAS ACT DOES NOT CONSTITUTE A SUBSTANTIAL IMPAIRMENT OF THE CONTRACTUAL RELATIONSHIP BECAUSE THE RELIANCE INTERESTS OF THE PARTIES WERE NOT FRUSTRATED.

In determining Contract Clause disputes, "the first inquiry must be whether the state law has, in fact, operated as a substantial impairment of a contractual relationship", *Allied Structural Steel*, 438 U.S. at 244. The analysis of this Court in that case reveals this Court looks to the expectation and reliance interests of the parties to the contract in assessing the amount of impairment. The foundation of the Contract Clause is that "government must keep its word"[34] and the parties are entitled to form their expectations of the basis of that word. If we examine the contract in this case from the viewpoint of what ERG reasonably expected at the time of the contract, it becomes clear that this contract was not impaired by the Kansas Act at all.

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[34] Tribe, *Constitutional Law*, p. 470 (1978).

A. The Expectation of the Parties Included Future State Legislation.

The basic starting point for an assessment of the impairment of a contract should be the words of the contract itself. In its brief, ERG is notably silent about the exact terms of its contract. An examination of those clauses reveals why. At the time of contracting both parties anticipated further state legislative action with regard to the terms of the contract, and incorporated any such future changes into their expectations. The relevant contract provisions read:

> "6.7 [8.5]. If any federal or Kansas regulatory or governmental authority having jurisdiction in the premises shall at any time hereafter fix a price per MCF applicable to any natural gas or any vintage produced in Kansas, higher than the contract price then in effect under this gas contract, the price to be paid for gas thereafter shall be increased to equal such regulated price. In that event, the increased price shall be effective as of the date of action of the governmental or regulatory authority establishing the regulated price, or its effective date, which ever is later, subject to the provisions of Section 8 [Section 10] hereof.[35]
>
> "18 [20]. GOVERMENT REGULATIONS
>
> "18.1 [20.1]. This gas contract shall be subject to all relevant present and future state and federal laws, decisions of any courts of law and equity, and all rules, regulations, and orders of any regulatory authority having jurisdiction. Neither party shall be held in default for failure to perform hereunder if

[35] Appendix to the Jurisdictional Statement, p. 66a (hereinafter referred to as J.S. A-p. §8).

> such failure is due to compliance with such laws, decisions, rules, regulations, or orders. This section will not operate to affect the rights and options granted to either party as provided for in Section 8 [Section 10] of this gas contract."[36]

These clauses clearly contemplate future state or federal regulation, including price regulation. The parties can have no expectation regarding the stability of state law when they expressly contract for changes in that law. The contract "contemplates exactly what came to pass"[37] and thus the state action did not impair the obligation of the contract.[38]

Chief Judge Frank Theis examined these very contract terms and the authorities and concluded that these contracts "fail to present a contract clause challenge", *Edmiston* v. *State Corporation Commission*, No. 79-1335 (D. Kan. Nov. 24, 1980), *slip opinion*, p.7; *see* discussion pages 4-7.[39]

The parties to a contract may agree with each other that the restraints of the contract will vary as the state law varies. The state becomes, in essence, a third party to the contract, with the power to unilaterally alter the terms of the contract. In such a case, it is impossible for the state

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[36] *Id.*, pp. 69a-70a.

[37] *National Building* v. *State Board of Education*, 85 N.Mex. 186, 510 P.2d 510, 512 (1973).

[38] *See also Vogel* v. *Tenneco Oil Co.*, 465 F.2d 563 (1972); *Austin* v. *Bennefield*, 140 Ga. App. 96, 230 S.E.2d 16 (1976).

[39] Hereinafter cited as *"Edmiston*, p.7". Judge Theis modified his opinion on Jan. 13, 1981 regarding the retroactive effect of the Kansas Act. *Appeal docketed*, No. 71-1197 (10th Cir. Feb. 23, 1981).

to impair the obligation of the contract. In this case, this Court should conclude that the Kansas Act was part of the expectation of the parties, and the contract is not impaired.

B. The Expectation of the Parties Did Not Reasonably Include the Section 102 Price.

ERG claims it "had every expectation that the price would continue to go up in the years to come" (Appt's Br. 25) citing other energy sources and the prospect of deregulation. ERG misstates the interest protected by the Contract Clause. Under the proper interpretation, the question is what the reasonable expectation of the parties was based upon the law at the time, as expressed in the contract. Under the contract, ERG could only expect an increase if some governmental authority established a price in Kansas higher than $1.50 plus 2¢ a year per MCF.[40] Even three years later, just before the NGPA, the national rate set by the FPC was still only $1.42 plus 1¢ a quarter per MCF.[41] The FPC national rate at the time of the contract was substantially less.[42] It was impossible even for very sophisticated observers to predict any future increases under the Natural Gas Act.[43] Thus, *even if* the law had stayed *exactly the same*, ERG had no fixed expectation interest.

ERG intimates that it expected deregulation (Appt's Br. 25). It is interesting to note that had complete deregu-

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[40] Sections 6.1 and 6.7 [8.1 and 8.5] J.S. App. 66a.

[41] F.P.C. Opinion 770-A, November 5, 1976 (18 C.F.R. 2.56a).

[42] Opinion 669-H, December 4, 1974, 52 F.P.C. 1604.

[43] Congressional Budget Office, Natural Resources and Commerce Division, *The Natural Gas Compromise*, August 2, 1978, pp. 5-6.

lation been established by Congress, ERG would have been stuck with the definite contract price, for there would have been *no* "higher . . . regulated price".[44] Paradoxically, ERG benefited more from the Kansas Act than it would have under full deregulation.

Even if ERG was precognitive enough to foresee and expect the NGPA, then its crystal ball should have also revealed Section 602 and the resultant Kansas Act. "Even if the passage of the [NGPA] could have been foreseen, state inaction could not have been foreseen."[45] In sum, ERG had no reasonable expectation at the time of the contract that any governmental body would establish any price much higher than the contract price.

C. The Reliance Interest of the Parties "Cuts Both Ways" so That KPL Could Rely on Moderate Prices.

"In some situations the elements of reliance may cut both ways", *Allied Structural Steel*, 438 U.S. at 246, fn. 18. This is such a case. In entering this contract, KPL relied on the law as it was at the time the contract was made. It could have relied on rates set "after agency proceedings, safeguarded by adversary participation and opportunity for judicial review".[46] The purpose of the Contract Clause is to "leave the parties to the law under which they contracted".[47] KPL's reliance interest was abrogated by the

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[44] Section 6.7 [8.5] J.S. App. 66a.

[45] *Edmiston*, p. 13.

[46] *Pennzoil Co.* v. *Federal Energy Regulatory Com'n*, 645 F.2d 360, 389 (1981).

[47] *Blaisdell*, 290 U.S. at 460 (Justice Sutherland, dissenting, quoting William Patterson of New Jersey).

NGPA.[48] Oklahoma and Kansas were merely trying to restore the parties to the *status quo ante*, while protecting the injured reliance interests of purchasers.

Thus, based on reliance and expectation interests, the state Acts should be upheld. "Laws which restrict a party to those gains reasonably to be expected from the contract are not subject to attack under the Contract Clause, notwithstanding that they technically alter an obligation of a contract."[49]

ERG had no expectation or reliance interest violated by the Kansas Act. The obligation of contract was only minimally impaired. "Minimal alteration of contractural obligations may end the inquiry at its first stage", *Allied Structural Steel*, 438 U.S. at 245. This Court should end its inquiry here, and base its opinion on the lack of an impaired obligation.

II. THE NGPA WAS AN UNFORSEEN AND UNFORESEEABLE EVENT WHICH ALTERED CONTRACT PROVISIONS TO THE DETRIMENT OF THE PUBLIC WELFARE.

The opinion of this Court in *Blaisdell*, 290 U.S. 398, has an extensive discussion of the "emergency" powers of a state, *e.g.*, 390 U.S. at 425-426; 439-442. The first *Blaisdell* factor is the existence of an emergency, 290 U.S. at 444. Later cases declared this emergency" factor as "subsumed in the overall determination of reasonableness" and not "regarded as essential in every case", *United States Trust*,

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[48] *Edmiston*, p. 12.

[49] *El Paso*, 379 U.S. at 497 (1965).

431 U.S. at 22-23, fn. 19.[50] More recent cases have apparently revised the "emergency" factor into testing whether unforeseen events have caused the original contracts to impact on the public in new, adverse ways.[51] The state "must show that it did not know and could not have known the impact of the contract on that state interest at the time that the contract was made", *United States Trust*, 431 U.S. at 32 (Burger, C.J., concurring).

Using this standard, the record before this Court is clear that the NGPA constituted an unforeseen development that altered contracts in a manner adverse to the public interest. Supporters of the Kansas Act called the NGPA a "radical reversal of federal policy" (J.S. App. 74a), and the Kansas Supreme Court concurred. "The NGPA constituted an entirely new and drastically different approach to the pricing of natural gas; it broke with the past, and substituted deregulation for close agency regulation . . ." (J.S. App. 22a). Neither Oklahoma nor Kansas knew or could have known of the revolutionary changes contained in the NGPA when these contracts were made in 1975. These changes do not create the power to alter contracts, but "afford a reason for the exertion of a living power",

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[50] *See also Viex*, 310 U.S. at 39-40; *East New York Savings Bank* v. *Hahn*, 326 U.S. 230 (1945).

[51] Thus in *El Paso* v. *Simmons*, this Court upheld a Texas law reposing land titles because the discovery of mineral wealth and developing problems connected with land held by speculators were "developments hardly to be expected or foreseen", 379 U.S. at 515 (1965). Conversely, in *United States Trust* v. *New Jersey*, this Court struck down a law repealing a state covenant because increased general concern regarding environmental protection and energy conservation were "not unknown" at time of covenant and did not cause it to have a "substantially different impact" on the public, 431 U.S. at 32.

Blaisdell, 290 U.S. at 426. Thus, utilizing this Court's recent standards, Oklahoma and Kansas had an appropriate situation for the exercise of their powers, and should be sustained in that exercise.[52]

III. THE STATE ACTS ADDRESS THE LEGITIMATE END OF DEALING WITH THE BROAD, GENERALIZED ECONOMIC PROBLEMS CREATED BY THE NGPA.

The second *Blaisdell* test was that the legislation was addressed to a "legitimate end", "not for the mere advantage of particular individuals but for the protection of a basic interest of society", 290 U.S. at 445. The *Allied Structural Steel* opinion called for the enactment to deal with a "broad, generalized economic . . . problem", 438 U.S. at 250. The Court traditionally has not looked behind the legislative determination unless a state contract and the states "self interest" is at stake, *United States Trust*, 431 U.S. at 26, or the act "clearly has an extremely narrow focus", *Allied Structural Steel*, 438 U.S. at 248.

ERG is trying to shoehorn this case into resembling the case in *Allied*, where only a pair of employers could possibly be affected by the specific conditions of the Minnesota law.[53]

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[52] Even under ERG's interpretation of the old *Blaisdell* standard, the State Acts could be sustained. The Oklahoma Legislature separately voted for a declaration of emergency, and the Kansas Supreme Court recognized the unforeseen nature of the NGPA. *Blaisdell* gave weight to declarations of emergency both by the Minnesota Legislature and the Minnesota Supreme Court, 290 U.S. at 444.

[53] The Act in *Allied* applied only to employers who: (1) had 100 or more employees; (2) at least one of whom worked in Minnesota; (3) which had established a voluntary pension plan; (4) had terminated his pension plan or closed his Minnesota office; (5) after April 10, 1974; and (6) before January 1, 1975. (438 U.S. at 248-249).

Here the interest of the public is broad and generalized, as evidenced by the fact that *three* separate sovereign *states* adopted parallel approaches to the NGPA. ERG is trying to make the Kansas Act a one-company law, totally ignoring the fact that KPL had nothing to do with the New Mexico or Oklahoma Acts.

From the Oklahoma perspective, it is hard to understand anyone questioning the legitimate, broad public purpose of the State Acts. The trial court said the legitimate public purpose could not be questioned (J.S. App. 19a). Chief Judge Theis in *Edmiston* identified two primary purposes of the Acts: to control natural gas prices, especially for public utility consumers, and to regulate windfalls.

The Kansas Act has presumably affected the thirty-seven percent of intrastate gas which had an indefinite price escalator clause in Kansas (J.S. App. 82a) and saved money for the 56% of the purchasers other than KPL (Appt's Br. 31). The Kansas Act has saved Kansas consumers over $128 million dollars (KPL draft brief, p. 36) with equal effect through the Kansas economy. By any standard, $128 million dollars is more than a "modicum". Saving that many millions clearly constitutes a legitimate end and a broad economic purpose.[54]

State legislatures may legitimately control intrastate gas prices, *Cities Service Gas Co.* v. *Peerless Oil and Gas*

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[54] Oklahoma is arguing the Kansas numbers because they are significant in their own right. They may unfairly seem less significant compared with Oklahoma's 65% of gas covered by indefinite price escalator clauses, enormous reliance on intrastate gas, and nearly a billion dollars in saving for consumers. Virtually every Oklahoman is affected by the Oklahoma Act. The smaller proportional effect in Kansas is still much larger than the miniscule effect in *Allied Structural Steel*.

Co., 340 U.S. 179 (1950). The prevention of windfalls is also a legitimate public purpose, *El Paso*, 379 U.S. at 515 (1965).[55] Congress explicitly recognized the legitimacy of state action in controlling indefinite price escalator clauses by the passage of Section 602 of the NGPA. Whatever else that section means, it clearly indicates that legislative action in this area is a legitimate action by a state.

Oklahoma in this brief gives the question of legitimate public purpose a summary disposition only because the question seems so clear to us. Oklahoma explicitly joins in the more lengthy discussions of this issue contained in KPL's brief and the brief of *amicus* Oklahoma Natural Gas, *et al.* The conclusion to all the argument is clear: the State Acts are directed toward a legitimate state end and broad, generalized public purpose.

IV. THE STATE ACTS ARE IN AN AREA ALREADY SUBJECT TO PRIOR STATE REGULATION AT THE TIME OF THE CONTRACT.

ERG virtually concedes that the Kansas Act was in an area already subject to state regulation but relegated that fact to a footnote as "irrelevant" (Appt's Br. 29, fn. 40). Oklahoma believes the establishment of the fact that this was an area subject to regulation at the time of the contract is relevant both to demonstrate that the contract was not significantly impaired, and to show the legitimacy of this particular exercise of the police power.

The test was stated in *Allied Structural Steel:* whether the act operated "in an area already subject to state regu-

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[55] "This Court's decisions have never given a law which imposes unforeseen advantages or burdens on a contracting party constitutional immunity against change."

lation at the time the company's contractural obligations were originally undertaken" 438 U.S. at 250, citing *Veix* v. *Sixth Ward Assn.*, 310 U.S. 32. In *Viex*, this Court stated the rule: "When he purchased into an enterprise already regulated in the particular to which he now objects, he purchased subject to further legislation upon the same topic", 310 U.S. at 38.

When ERG entered the natural gas field, it should have known it was entering an intensely regulated industry. In Oklahoma, natural gas prices have been subject to Corporation Commission control since 1913, 52 O.S. 1981, §§ 52, 53. Clear evidence of Kansas' known ability to regulate in this area is provided by the contracts themselves, which speak of a "Kansas regulatory or governmental authority" setting prices (J.S. App. 66a) and "present and future state law" (J.S. App. 69a-70a), regulating the conduct of the parties. ERG "purchased into" an area it knew was regulated, and now complains when it is in fact regulated. This Court should recognize that prior state regulation in this area gave ERG ample warning that the state would not sit quietly when the public interest was adversely affected.

V. THE STATE ACTS HAVE REASONABLE CONDITIONS AND ARE OF A CHARACTER APPROPRIATE TO THEIR PUBLIC PURPOSE, FOR THEY ARE CAREFULLY PATTERNED AFTER THE NGPA.

This Court summarized the relevant rule for private contracts in *United States Trust*, 431 U.S. at 22-23:

> "Legislation adjusting the rights and responsibilities of contracting parties must be upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption. As is customary in review-

> ing economic and social regulation, however, courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure." (citations omitted)

ERG grants the states no deference in their legislative judgment, but attempts to list what it sees as viable alternatives to the considered decisions of three legislatures. If we recall that the objectives of the legislation are to protect natural gas purchasers from unanticipated price hikes and prevent windfall profits to producers, it is easy to dispose of the proffered "alternatives".

ERG suggests that the states could have refused to allow utilities to pass through the higher cost of gas (Appt's Br. 37). This action might protect consumers in the short run, but would not have adjusted the windfall for producers. Furthermore, it would have had the effect of denying the utilities compensation for their expenses, which could lead to a claim of deprivation of property without due process, as guaranteed by the Fourteenth Amendment, *Bluefield Water Works* v. *Public Service Com'n.*, 262 U.S. 679 (1923); *FPC* v. *Hope Natural Gas*, 320 U.S. 591 (1944). In addition, in the long run it might cost ratepayers more, for few utilities could stay out of bankruptcy court if their stockholders were to be forced to swallow a proportionate share of a billion dollar outflow.

ERG's second alternative is to shift the expense of the higher costs to industrial customers through "incremental pricing". This alternative fails both primary objectives of protecting *all* ratepayers from rate jumps, and once again does not alter the windfall income of producers.

ERG complains that the Acts allow for voluntary renegotiation of contracts (Appt's Br. 39-40). Oklahoma wonders if ERG would truly have been happier with an act that *prohibited* renegotiation. Under such a provision, *both* parties might be stuck in an agreement that each wanted to change, but be prohibited by law from doing so. Under such a scenario, we might have some *serious* constitutional challenges to such a law.

ERG asserts that the Acts lack the temporary nature found important in *Blaisdell* (Appt's Br. 39). The Acts are conceded to have a termination date which coincides with the termination of the NGPA. Claims that the *impairment* is permanent are necessarily based on the conclusion that there is significant impairment. Since ERG had no reason when it made the contracts to expect a windfall, it loses nothing when the windfall does not come.

Finally, we come to the question of whether indefinite price escalator clauses are against public policy. ERG recites that Kansas has not restricted them; KPL has agreed to them; and the NGPA was meant to trigger them. Unnoted by KPL is the fact that the Acts continue to give such clauses an active role. They still work; just not to the explosive extent that they might have. The Legislatures are directed to use means "of a character appropriate to the public purpose", *United States Trust*, 431 U.S. at 21. This Court has recognized that indefinite price escalators can legitimately be found to be against public policy, *Permian Basin Area Rate Cases*, 390 U.S. 747, 782 (1968). Since the state legitimately could prohibit their entire existence, they are very suitable material for lesser regulation in the public good. Through the Acts, the indefinite price escalator

clauses are tamed to gradually introduce energy price increases into the state economy. This Court has recognized that a gradual approach may also be a factor in assessing the reasonableness of a legislative act, *Allied Structural Steel,* 383 U.S. at 247.

The Oklahoma Legislature carefully tailored the Oklahoma Act to conform to the situation before it and the precedents of this Court. The result was a reasoned and careful response to the situation, with constant legislative monitoring of the effects and results. After equally careful consideration, this Court should affirm the efforts of the Oklahoma and Kansas legislatures.

CONCLUSION

The ultimate question contained in this case for the Court is: What is the nature of the Contract Clause nearly two centuries after it was drafted? We know it is not a "mathematical formula", *Blaisdell,* 290 U.S. at 428. We know it is not a "dead letter", *Allied Structural Steel,* 438 U.S. at 241. We know it has not been "balanced away", *United States Trust,* 431 U.S. at 29, but the police power can not be bargained around, *Hudson Water Co.* v. *McCarter,* 209 U.S. 349, 357 (1908). What, then, *does* it mean?

The Contract Clause is a process, a series of tests for suspected offending state legislation. First, we test to see if there is any impairment at all, looking to the language of the contract, the reasonable expectation of the parties, and the language of the act. If there is no impairment, then our examination is at an end.

If there appears to be some impairment, we evaluate the amount of impairment. If it is very slight, once again we end the examination. If the impairment is more than slight, then we must look to the reason why the act was passed and whether the act is unreasonable in light of those reasons.

It is a valid reason if the act is in response to an unforeseen occurrence which has caused private contracts to be hurtful to the public good. It is not a valid reason if the act is for the benefit of the few, rather than the many; if it is in the state's selfish interest; or if it is designed to destroy the contractural obligation. If the protection of the act does not serve a legitimate interest, then the means to effectuate it are automatically unreasonable.

If the protection of the act serves a legitimate interest then we must examine the means by which the act seeks to afford such protection. If the act is itself an unforseen calamity; if it is instant burden, rather than gradual; if it is perpetual, then it may be an unreasonable response on the legislature's part.

If we examine the Oklahoma and Kansas Acts by these standards, they do not violate the Contract Clause. The Acts do not impinge upon the reasonable expectation of the parties, or if they do, it is slightly. The protection of the act is not of a forbidden type, but rather is for the benefit of the majority of Kansans and Oklahomans. The protection is implemented in an area where the state has acted before. The methods are gradual, and the Acts are temporary. The Acts are careful responses to difficult and complex situations, and should therefore be approved by this Court.

Respectfully submitted,

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No. 81-1370

In the Supreme Court of the United States

October Term, 1982

ENERGY RESERVES GROUP, INC.,
Appellant,

vs.

THE KANSAS POWER AND LIGHT COMPANY,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF KANSAS

APPELLEE'S OPPOSITION TO MOTION OF OKLAHOMA PRODUCERS FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* OUT OF TIME IN SUPPORT OF APPELLANT

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SUMMARY OF OPPOSITION

Appellee The Kansas Power and Light Company ("KPL") submits this memorandum in opposition to the motion of the Energy Consumers and Producers Association, Oklahoma Independent Petroleum Association, Service Drilling Company, Harrison L. Townes, Inc., Southland Drilling and Production Company, L. O. Ward, and Amerada Hess Corporation ("Oklahoma Producers"), filed September 3, 1982, for leave to file a brief *amicus curiae* out of time in support of appellant.

Supreme Court Rules 36.2 and 36.3 prohibit the untimely filing of an *amicus curiae* brief. According to the

rules, the Oklahoma Producers' motion for leave to file shall not be received unless submitted within the time allowed for appellant's brief. The Oklahoma Producers filed their motion on September 3, 1982—almost three months after the June 12, 1982 expiration of the time permitted appellant for briefing, and almost three weeks after KPL filed its Brief for Appellee on August 14, 1982. Consequently, KPL lacks a fair and adequate opportunity to address this additional brief.

Furthermore, the Oklahoma Producers have long been aware of this litigation and knew more than two months ago that certain Oklahoma utilities and the Oklahoma Corporation Commission would file briefs *amicus curiae* supporting appellee KPL. The Oklahoma Producers could easily have moved to file timely these briefs or sought the consent of all parties. Accordingly, the Court should not grant leave to Oklahoma Producers to file out of time.

OPPOSITION TO MOTION

I. This Court's Rules Do Not Permit Oklahoma Producers to File a Brief *Amicus Curiae*

If a nonparty seeks to file an *amicus curiae* brief without the consent of all parties to a case, Supreme Court Rule 36.3 requires the nonparty to seek leave of court by motion. The rule further states, "No such motion shall be received unless submitted within the time allowed for the filing of an *amicus* brief on written consent." Rule 36.2 establishes the time allowed for the filing of an *amicus* brief on written consent as the time allowed for the filing of the brief of the party supported. The Oklahoma Producers seek leave to submit their brief in support of the appellant, but appellant's brief was due and was filed on June 12, 1982—almost three months ago.

Furthermore, Supreme Court Rule 36.2 expressly prohibits an *amicus* who supports the appellant from filing a reply brief to the positions of the appellee and *amici* supporting the appellee. By postponing their *amici* participation until after all briefs for appellee are filed, the Oklahoma Producers here seek to do precisely that.

The Oklahoma Producers directly confront both Rules 36.2 and 36.3 by attempting to file their brief in support of appellant and as a reply to the *amici* briefs that support the appellee. The only authority on which the Oklahoma Producers rely, however, addresses the propriety of non-party opposition to a motion for leave to file a brief *amicus curiae*.[1] The brief of the Oklahoma utilities, to which the Oklahoma Producers respond, was filed by the consent of the parties and is not before the Court on motion.[2] Indeed, the *amicus* brief of the Oklahoma Corporation Commission, which was presented to this Court by motion for leave to file, was sponsored by the Attorney General of that state and likely did not require that motion for filing.[3]

Clearly the Supreme Court Rules permit the filing of *amicus* briefs within strict time limits so that parties opposing the arguments posed in those briefs may have an opportunity to respond. The Oklahoma Producers' motion and attached brief should have been filed in June. KPL would then have had an adequate and fair opportunity to respond to the erroneous contentions raised.

Accordingly, the receipt of the Oklahoma Producers' motion is not permitted by the Court's rules.

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1. R. Stern & Gressman, *Supreme Court Practice* §13.13 at 727 (5th ed. 1978).

2. *See* Brief *Amicus Curiae* of Oklahoma Natural Gas Co., et al., at 1 n.1.

3. *See* Supreme Court Rule 36.4.

II. The Oklahoma Producers Were Aware of This Litigation and the Intent of the Oklahoma Corporation Commission and Oklahoma Utilities to File Briefs *Amicus Curiae* in Support of Appellee's Position and Could Have Timely Filed Their Brief

The Oklahoma Producers share in this litigation the identical interests of Appellant Energy Reserves Group, Inc. ("ERG"). The Oklahoma Producers sell intrastate natural gas in Oklahoma pursuant to contracts with indefinite price escalation clauses, which are restricted by the Oklahoma Natural Gas Price Protection Act. The Oklahoma Act is the predecessor statute to the Kansas Natural Gas Price Protection Act that ERG challenges here. In actions pending in federal court in Oklahoma since March 1979, the Oklahoma Producers similarly challenge the Oklahoma Act as an allegedly unconstitutional impairment of their ability to obtain higher natural gas prices pursuant to their intrastate gas purchase contracts.

The Oklahoma Producers claim that until receipt of the briefs of *amici* supporting KPL, they "perceived no cause for seeking to be heard in this appeal" and that "[m]atters raised by the Oklahoma [*amici* supporting KPL] impact directly upon issues in the Oklahoma cases . . ."[4] These claims belie the Oklahoma Producers' close observation of, and participation in, the Kansas litigation that paralleled the constitutional challenge to the similar Oklahoma Act. The Oklahoma Producers previously were clearly aware of this case and the *amici* participation from the Oklahoma utilities and Corporation Commission. Both the Oklahoma Producers and the utilities have participated as *amici* in the companion federal court challenge to the

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4. Motion of Oklahoma Producers for Leave to File Brief at ii.

Kansas Act, now pending in the Tenth Circuit Court of Appeals.[5]

The Oklahoma Producers knew that ERG's appeal would control the disposition of their Oklahoma challenge. ERG's Jurisdictional Statement expressly argued that disposition of this appeal would "give needed guidance" both to the Oklahoma federal courts, where the Oklahoma Producers pursue their similar challenge,[6] and to the United States Court of Appeals for the Tenth Circuit, where numerous Kansas producers are pursuing their constitutional challenge against the Kansas Act.[7] Indeed, the Oklahoma Producers' challenge to the Oklahoma Act has been stayed pending this appeal.[8]

The Oklahoma Producers demonstrated their previous awareness that a higher federal court ruling on the constitutionality of the Kansas Act would affect their interests. On January 11, 1982, these producers, as represented by the Oklahoma Independent Petroleum Association, filed a brief *amicus curiae* in the Kansas litigation now pending in the Tenth Circuit, and there supported the position of the Kansas producers challenging the Kansas Act. The same Oklahoma utilities participating here had also filed an *amicus* brief in *Edmiston* supporting the position of the Kansas Corporation Commission and KPL. The same Oklahoma participation here is hardly a surprise to the Oklahoma Producers.

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5. *See Edmiston v. State Corp. Comm'n*, No. 79-1335, Slip Op. (D. Kan. Nov. 24, 1980), *as modified, id.* (D. Kan. Jan. 13, 1981), *appeal docketed*, No. 81-1197 (10th Cir. Feb. 23, 1981).

6. *Energy Consumers and Producers Ass'n v. Baker*, Nos. 79-320-D & 79-823-D (W.D. Okla., filed March 20 and 27, 1979).

7. J.S. 25 n.37.

8. Motion of Oklahoma Producers for Leave to File Brief at ii.

The Oklahoma Producers were fully aware that Oklahoma and the Oklahoma utilities would file briefs *amicus curiae* in this Court supporting the appellee. Even if the Oklahoma Producers could not so deduce from the *Edmiston* participation, Oklahoma trade journals had announced the fact more than a month before the briefs were filed. On July 7, 1982, the Oklahoma Energy Environment Report, a trade publication with wide circulation in the natural gas industry in Oklahoma, reported that a coalition of Oklahoma utility companies and the Oklahoma Corporation Commission would file "separate advisory briefs" in this litigation.[9] The text of that article has been reproduced in an appendix hereto. This article was available to the Oklahoma Producers more than five weeks before KPL filed its Brief for Appellee in this litigation. The Oklahoma Producers, however, deliberately made no attempt in this interim period to seek leave to file an *amicus* brief that would still afford KPL an opportunity to respond.

KPL already had indicated its willingness to consent to *amicus* participation supporting appellant, when sought in a proper and timely fashion that afforded KPL an opportunity to respond. Other nonparties sought and obtained the consent of KPL to file briefs *amicus curiae* supporting ERG's position, but later chose not to file those briefs.[10]

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9. Oklahoma Energy Environment Report No. 27 at 56 (Oklahoma Business News Co. July 7, 1982); *See* Appendix.

10. The Legal Foundation of America requested and obtained, pursuant to Supreme Court Rule 36.2, consent from KPL to file a brief *amicus curiae* supporting appellant's position. On June 12, 1982, the Foundation informed KPL by letter that it would not file the initially proposed brief. The Foundation had already filed an *amicus* brief in the *Edmiston* litigation in the Tenth Circuit. See Brief *Amicus Curiae* of the Legal Foundation of America, *Edmiston v. State Corp. Comm'n, supra* note 5.

The only reason for delay in filing this *amicus* brief is the explicit decision by the Oklahoma Producers to file their *amicus* brief only after all briefs for appellee have been filed. This conduct would permit the Oklahoma Producers to support appellant's position with a reply brief to which KPL has no adequate opportunity to respond.

CONCLUSION

Appellee KPL respectfully submits that the proposed brief *amicus curiae* of the Oklahoma Producers is three months out of time and, by supporting appellant's position, denies KPL an adequate and fair opportunity to respond to its contentions. KPL respectfully submits that the motion for leave to file this brief should be denied.

Respectfully submitted,

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APPENDIX

EXCERPT FROM OKLAHOMA ENERGY ENVIRONMENT REPORT, Vol. 12, No. 27 (Oklahoma Business News Co., Oklahoma City, Oklahoma, July 7, 1982)

STATE UTILITIES, CORPORATION COMMISSION JOIN IN GAS PRICING CASE

A coalition of Oklahoma utility companies and the Oklahoma Corporation Commission plan to file separate advisory briefs with the U.S. Supreme Court in a case involving a state's ability to place pricing limitations on flowing natural gas already under contract.

Styled *Energy Reserve Group Inc. v. Kansas Power and Light,* the case is an appeal from a Kansas Supreme Court decision upholding the constitutionality of a Kansas statute which limits the action of price escalator clauses in natural gas contracts.

The Kansas law is modeled on a similar Oklahoma statute, with changes for differences reflecting the various types of contracts in the two states.

Oklahoma, for example, has more intrastate natural gas under contracts involving favored nation and price escalator clauses, while Kansas purchasers were buying more gas under contracts containing area rate clauses.

Utilities Advise Court of Public Interest

Joining the utility brief are: *Oklahoma Natural Gas Co., Oklahoma Gas and Electric Co., Public Service of Oklahoma* and the rural electric cooperatives. The coalition has retained Washington, D.C., counsel to assist in preparing the amicus curiae (friend of the court) brief.

The coalition does not intend to petition as an intervening party in the case, but would strictly file a brief

to advise the court of the Oklahoma statute and its affect [sic] on the public.

Major issue addressed by the coalition is expected to be the constitutionality of a state, by statute, impairing existing contracts, in this case the ability of a state to cripple the price escalator clauses.

The Oklahoma Corporation Commission plans to file a separate brief in the case.

Robert Stewart, commission general counsel, explained the major purpose of the brief would be to point out the factual distinctions that exist between circumstances surrounding the Kansas case and a pending challenge of the Oklahoma statute. The commission is hopeful the court's decision will not jeopardize the commission position in the Oklahoma case.

Oklahoma Under Challenge in Federal Court

The Oklahoma case challenges the constitutionality of a 1979 state law (passed as *SB 49*) which limits the action of price escalator and favored nation clauses within natural gas contracts.

Basically, these clauses call for the contract to be periodically reviewed and prices increased to match the highest price being paid in a designated area.

Different types of clauses are triggered by a variety of factors including: the highest price being paid by a particular purchaser within the region; the highest price being paid by any purchaser within a designated area, or an increase in the allowable price on certain types of government price regulated gas.

The Oklahoma statute limits how rapidly prices may be increased under these clauses by setting a ceiling on the annual amount of escalation, tied to increases allowed under the federal Natural Gas Policy Act of 1978.

Immediately after passage, the constitutionality of the new state statute was challenged by two federal lawsuits, one filed in the northern and one in the western district. The northern district case was later transferred to the western district and both cases were consolidated before Judge Fred Daugherty where they have been pending at issue since October 1980.

Kansas Models Statute on Oklahoma Law

Following passage of the Oklahoma statute, principal architect Sen. Gene Howard, Tulsa, and others traveled to Kansas to address committees of that state's legislature on provisions of the new act.

In May 1979, the Kansas Legislature passed a bill modeled on the Oklahoma statute. The constitutionality of the Kansas law was challenged both in federal and state courts.

To date, the bill's constitutionality has been upheld by the Kansas Supreme Court and by the federal district court for the State of Kansas. The federal court decision is now on appeal to the 10th Circuit Court of Appeals.

Since Oklahoma is also within the 10th circuit, a decision from this court addressing the broader underlying issues of the Kansas case could virtually render moot the cause pending in Oklahoma.

Oklahoma Natural Gas Co., one of the principal participants in the Oklahoma litigation has written the 10th circuit appeals court advising of the broader public interest in the Kansas case.

Briefs Due in July

The Kansas Supreme Court ruling on the law is now pending before the U.S. Supreme Court on appeal. Energy Reserve Group has already filed briefs. The brief from

Kansas Power and Light is due July 15, but the utility has requested a two-week extension.

The amicus briefs from the coalition of Oklahoma utilities and the state corporation commission will be due at the same time as the Kansas Power and Light brief. Energy Reserve Group will then have an opportunity to file a reply brief.

The court is expected to schedule oral arguments in the matter when it reconvenes in October. Presently, oral argument seems likely in November with no decision expected until after the first of the year.

The utilities and Oklahoma commission are involved as major purchasers and the regulatory agency for the state.

Statute Could Save Oklahomans $1 Billion

Since Oklahoma public utilities are the major purchasers of natural gas within the state any price increases would be passed along to consumers.

At the time of the law's passage ONG, PSO, and OG&E estimated that without the new statute Oklahoma utility ratepayers would be charged an additional $1 billion by 1985, the law's expiration date.

Should the statute eventually be overturned, a 1980 state law allows the purchasers to repay in monthly installments the amount which accumulated during the litigation process.

These monthly installments will be based on equal monthly payments divided over the same number of months as the time from the passage of the law until the final court decision. The amount would be repaid at 10 percent interest.

Docket Sheet

NO. 81-1370-ASX	TITLE Energy Reserves Group, Inc., Appellant v. The Kansas Power and Light Company

DOCKETED	COURT
Jan. 21, 1982	Supreme Court of Kansas

DATE	PROCEEDINGS AND ORDERS
	Counsel for Appellant: Gary W. Davis
	Counsel for Appellee: Jerome T. Wolf,
Dec. 10, 1981	Application for an extension of time to docket an appeal and order granting same until January 21, 1982 by White, J, on Dec. 11, 1981.
Jan. 21, 1982	Statement as to jurisdiction filed. (Record filed).
Jan. 21, 1982	Appendix filed.
Feb. 10, 1982	Order extending time to file a motion to dismiss the appeal until March 5, 1982.
March 8, 1982	Motion to dismiss filed.
March 10, 1982	DISTRIBUTED. 3-26.
Mar. 12, 1982	Motion of State Corporation Commission of the State of Kansas for leave to file a brief as amicus curiae filed.
Mar. 16, 1982	Reply brief for the appellant filed. (D).
Mar. 19, 1982	Appellant's opposition to motion of The Kansas Corporation Commission to file a brief as amicus curiae filed. (D).
Mar. 23, 1982	DISTRIBUTED. 3-26. (Motion for leave to file amicus brief)
Mar. 29, 1982	The motion of State Corporation Commission of Kansas for leave to file a brief as amicus curiae is GRANTED. Probable jurisdiction is NOTED.

Apr. 20, 1982	Order extending time to file the joint appendix and appellant's brief on the merits until June 3, 1982.
May 20, 1982	Order FURTHER extending time to file the joint appendix and appellant's brief on the merits until June 12, 1982.
June 11, 1982	Joint appendix filed.
June 11, 1982	Brief for the appellant filed.
June 29, 1982	Order extending time to file the appellee's brief on the merits until July 29, 1982.
July 15, 1982	Order further extending time to file the appellee's brief on the merits until Aug. 14, 1982.
Aug. 13, 1982	Brief for the appellee filed.
Aug. 13, 1982	Brief, amici curiae of Oklahoma Natural Gas Company, et al. filed.
Aug. 13, 1982	Brief, amicus curiae, of State Corporation Commission of the State of Kansas in support of appellee filed.
Aug. 16, 1982	Brief, amicus curiae of Oklahoma Corp. Commn. filed.

OVER

81-1370

Title

No.

DATE	PROCEEDINGS AND ORDERS
Aug. 16, 1982	Brief, amicus curiae of Kansas Legal Services, Inc. filed.
Sept. 3, 1982	CIRCULATED.
Sept. 3, 1982	Motion of Energy Consumers and Producers Association, et al. for leave to file a brief as amici curiae filed.
Sept. 11, 1982	Appellee's opposition to motion of Oklahoma Producers for leave to file brief amicus curiae out-of-time filed.
Oct. 4, 1982	The motion of Energy Consumers and Producers Association et al. for leave to file a brief as amici curiae is DENIED.
Oct. 22, 1982	Reply brief for the appellant filed. (D).
Nov. 9, 1982	ARGUED.